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PREFACE TO FIRST EDITION.

ALTHOUGH the present volume has considerably exceeded the limits originally arranged between myself and the publishers, I cannot but feel that the vast subject to which I have addressed myself is very far from being exhaustively treated in the following pages. In particular, I feel that the chapter dealing with the audit of different classes of undertakings is, in spite of its considerable length, very far from complete; and, further, I regret that space has altogether failed me for a more full discussion of the various legal decisions that affect the duties and responsibilities of the profession.

On the other hand, I venture to hope that the present attempt to combine, within the limits of a volume of convenient size and reasonable price, the leading principles that should guide the Auditor in the course of his investigations, together with the special points that require his consideration in the case of any particular concern, will be found not only of value to the Accountant Student—whose opportunities of gaining experience are, naturally, somewhat limited—but also of some utility to practising members of the profession, both in the ordinary course of their daily routine, and also—more especially—when they find themselves face to face with the accounts of a business with which they have hitherto been unfamiliar.

If it should be thought that the standard I have throughout advocated is somewhat Utopian in character, and unattainable

in practice, I can only reply that I maintain that, to me, an incomplete investigation seems worse than useless ; and I am convinced that it is only by voluntarily accepting, and even increasing, the responsibilities of our position that we can hope to maintain and to increase the large measure of public confidence we at present enjoy.

It would be impossible for me to specifically acknowledge my indebtedness to all the various members of the profession whose valuable opinions have so materially assisted me in the production of this work ; but none the less, I desire to thank them most cordially for the benefits I have received from their experience.

In conclusion, I would wish to add that, as I have laid no claim to completeness in this work, so also do I wish to disclaim any assumption of absolute finality ; and, accordingly, I shall consider myself greatly indebted to my readers for any suggestions and opinions with which they may be pleased to favour me, which, I need hardly add, shall receive every attention upon the publication of a new edition.

LAWRENCE R. DICKSEE.

13th July 1892.

PREFACE TO SEVENTH EDITION.

THE Sixth Edition of this work being now exhausted—representing a sale of 7,000 copies—it has become necessary to prepare a Seventh.

Advantage has been taken of this to carefully revise the whole of the text, and to re-write or re-arrange those portions that have been affected by recent legislation or decisions. At the same time a determined effort has been made to avoid further increase in the size of the work, with the result that it has been found possible to effect a saving of some sixteen pages in the body thereof, without (it is hoped) omitting anything of value; while, on the other hand, much new matter will be found under the headings of Depreciation, Local Authorities' Accounts, Secret Reserves, and other matters that have recently attracted attention. In the Appendices certain additions have of necessity been made to the extracts from Acts of Parliament, and reports of all important cases since the last edition was issued have been added to Appendix "B": on the other hand, one or two cases of minor importance have now been omitted. A new Appendix—"E"—appears in this edition, dealing with the more important clauses of the Companies Bill now before Parliament, and discussing their probable effect upon the position of Auditors, should they be enacted in their present form.

It has been a source of great satisfaction to the Author to observe that the sales of this work show that, while it continues to be regarded with steadily increasing favour by

professional accountants in all English-speaking countries, there appears to be a growing demand for it among business men and economists, both at home and abroad. The increased attention that is being given to this important subject of late years outside the ranks of professional accountancy will, there is little doubt, prove of great and lasting value.

In the United States of America the demand for this work, which has always been favourable, has of late so increased as to justify the issue of a special American Edition. This has been prepared under the Author's supervision by Mr. Robert H. Montgomery, C.P.A., and published at New York in September 1905. At the time of writing the first "American" edition, of 1,000 copies, has been practically exhausted; a reprint is now in the press, and a second (and revised) edition is now in active preparation. It is satisfactory to observe that, while the local conditions in the States make much contained in the present volume inapplicable, the principles of auditing and the practice of professional accountants throughout the world are sufficiently uniform to enable this work to rank as a standard text-book in both hemispheres.

The Author gladly takes advantage of the opportunity afforded by this Preface to express his indebtedness to numerous members of the profession for valuable suggestions received in the past, and to express the hope that a similar kindness will be extended to him in the future.

LAWRENCE R. DICKSEE.

48 *Copthall Avenue, London, E.C.*

15th April 1907.

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ERRATA.

Page 289, line 17; *for* "South Africa," read "South America."

Page 402, after line 18; It should be noted that, in the course of his Budget speech on the 18th April 1907, the Chancellor of the Exchequer intimated that an allowance of 3d. in the £ (in addition to all existing allowances) would be made upon all "earned" incomes not exceeding £2,000 per annum. At the same time an increase in the rate of Estate Duty on estates exceeding £150,000 was announced.

A U D I T I N G .

CHAPTER I.

INTRODUCTORY.

AUDITING (up to the Trial Balance).

PRELIMINARY CONSIDERATIONS.—The first point that claims attention is the method, or system, upon which an audit should be conducted; and here on the outset, one is brought face to face with some very considerable differences of opinion and practice among members of the profession.

It is mentioned by Mr. G. P. NORTON, F.C.A., that the practice of his firm (Armitage & Norton) is to have "certain printed instructions of a general character which are bound in small note-books, together with a number of spare blank leaves for memoranda. At the commencement of a new audit one of the note-books is appropriated to it, and the general instructions are carefully revised and special instructions supplemented. The clerk who has this book with him is thus shown precisely what are his duties with regard to the audit upon which he is engaged." The late Mr. C. R. TREVOR, F.C.A., in a lecture of somewhat earlier date, advocated a similar practice. He said: "The practice of having an Audit Book for each audit is highly important, with columns for the initials of each person who has performed the work, and made himself responsible for its having been correctly and thoroughly done. By this means much labour is saved on a second audit, and thorough continuity secured." It may be noticed that Mr. TREVOR made no mention here of any "instructions," but his remarks clearly pre-suppose the Audit Book to contain a definite list of duties to be performed.

Since the issue of the first edition of this work the author has published an "Audit Note-Book," the demand for which is sufficient to prove that the use of such a book is very general among the profession.

On the other hand, it has been suggested "that if a competent clerk is sent to undertake an audit (and none but competent clerks *should* be sent), it is much the better way to leave him unfettered with printed instructions, but allow him to go thoroughly into the whole system in operation, and from the nature of such system, and from what he sees, let him outline his own method of procedure. By this means there is not so much danger of his getting into a semi-careless groove of working, and moreover he feels that more responsibility is placed upon him, which acts as an incentive to do the work more thoroughly than would be the case were he working to 'rule of thumb.'" There is, doubtless, something to be said upon this side of the question; but if so much be left to the clerk, it is a little difficult to see what the principal is expected to do himself. In any case, however, the book is useful as a record of the routine work performed and of the queries raised in the course of audit. It is believed that, in point of fact, some sort of Audit Note-Book is almost invariably used by most accountants at the present time.

The late Mr. DAVID CHADWICK, F.C.A.—after an experience of upwards of fifty years—was distinctly in favour of a stereotyped set of instructions. The set used in his office (which is given below) is especially full and complete; and although, of course, but a mere indication of an Auditor's duties, it will be found extremely suggestive:—

INSTRUCTIONS FOR AUDIT.

1. In commencing a new audit you should obtain a list of all the books kept, and of all persons authorised to receive or pay money and order goods.
2. In the case of a joint stock company, examine the articles and board minutes respecting the receipt and payment of money, and the drawing of cheques, acceptances, &c.

3. Ascertain and take note of the general system upon which the books are constructed, and the plan of checking the correctness of the accounts paid, and whether exclusively or generally by cheques.

4. Report if the accounts and vouchers have been submitted to the board of directors by an account committee or otherwise, and whether they have been systematically checked and certified; and note any discrepancies.

5. Examine all the items in the Cash Book with the Bank Pass Books and vouchers, and put your usual audit initials in the Pass Book and to every item in the Cash Book. Ascertain if the Bankers' Pass Book is frequently entered up and examined.

6. Note any unusual or extraordinary payments or receipts.

7. In regard to the payments for wages and petty cash, note any unusual items, and see that vouchers for all payments are kept and produced.

8. Report whether a rough Cash Book is kept, and whether the fair Cash Book is regularly and punctually posted and balanced, and if the balance is checked.

9. Report also if the entries in the fair Cash Book are in arrear, on account of the current year; and if so, to what extent, and why.

10. In all cases where branch establishments are included in one business you will be careful to examine into the mode of bringing the returns of work, accounts, and expenses to the head office.

11. Examine all the Day Books, and see that the proper returns of purchases and sales are made by each department, and that the Bought and Sold Books are properly entered up; that the invoices are properly checked as to quantities and prices; obtain a declaration, or otherwise satisfy yourself, that every liability of the year is brought into account.

12. The postings in the Personal Ledgers must be checked from the Bought and Sold Day Books and the Cash Book, and also from the Bill Books and Journal.

13. The postings in the Nominal or Impersonal Ledgers must be checked from the journalising of the Bought and Sold Day Books, the Bill Books, the Invoice Books, and the Cash Books, and the mode and correctness of the journalising must be carefully proved.

14. Examine the Bills Receivable and Bills Payable Books, and note any item of past due, renewed or dishonoured bills, and make list of same and of the securities, if any.

15. Examine the entries and transfers passed through the Journal, and check the postings; and although you are not held responsible for the details of classification, it is desirable you should make any suggestions required, and note any discrepancies, especially in relation to the division of expenditure on account of Capital and Profit and Loss Accounts respectively.

16. Examine the Share Register, and see that the amounts received for calls agree with the entries in the Bank Pass Books, and that they are correctly posted to the credit of the respective shareholders in the Share Ledger: that all transfers from the transfer deeds are duly stamped and entered in the Register of Transfers; and also that the amount of the subscribed and paid-up capital and arrears corresponds with the Balance Sheet.

17. Examine the register of all mortgages on the company's property, and all debenture bonds issued, and note and check the amount of capital paid in advance of calls, and of the receipts and payments in respect thereof with the Bank Pass Book.

18. In the accounts of stock-taking see that all stock sheets and returns are duly signed by the heads of departments, and that the same are correctly carried forward to the General Stock Account; and ascertain and note whether goods finished or in progress are taken at cost price or otherwise; also report whether in large concerns an independent check clerk or valuer has verified the stock returns in regard to prices and quantities.

19. In checking the Profit and Loss Account, note whether the usual and proper deductions are made for wear and tear and depreciation, and for recouping of capital on works or premises held on short leases.

20. Take care that in the Balance Sheet no additions are made to expenditure on Capital Account, except such as are duly authorised by the board of directors, and note the distinction between new works and mere replacements.

21. Ascertain whether the conveyance deeds and other securities specified in the agreement of purchase and articles of association have been duly executed, and the sums paid by the company on account of purchase have been duly endorsed thereon or otherwise acknowledged to the satisfaction of the solicitors or board of directors; also that the existence and safe custody of these documents have been duly certified; ascertain by application to the bankers the correctness of any balances, bills, or securities lodged with them.

22. Ascertain the correctness of the cash balances, bills, and other securities in hand, and take note of every exceptional transaction.

To sum up, then, the matter may be stated thus:—At the commencement of an audit the principal should, if possible, go over the ground personally, and decide what work requires to be done. A list of such work (together with any other special notes that may seem desirable) should be entered in the Audit Note-Book, which should be ruled in columns, so that the initials of a clerk against any item may clearly show that he is responsible for the correctness of that item for the period named at the head of the column. In most cases it is practicable to keep books ready printed which, with but slight alteration, will answer the purposes of any audit; but there will usually be some special circumstances connected with each audit that distinguish it from others, and these circumstances will usually involve some modification of the customary routine obtaining to that class of accounts.

Some sort of definite system is undoubtedly preferable to leaving things too much in the hands of the audit clerk, as there is, in the latter case, always a danger, either of dissatisfying the client, or else of leading him to prefer a change of principals to a change of clerks, if one of the two be inevitable. For this reason, if for no other, the principal should always endeavour to keep the reins of every audit in his own hands, or, at least, out of the exclusive control of any one audit clerk; for, although objection may legitimately be taken to the latter being kept at a continual game of "General Post," it cannot be denied that it is a mistake to invariably send the same clerks to the same audits.

Before leaving the question of Audit Note-Books, attention may be directed to the following, which is employed in the office of Messrs. G. N. READ, SON & CO., F.C.A.:—

AUDITING.

Date	Cash Balanced	Bank Balance agreed	Cash Book Vouchers	Bought Ledger Vouchers	Petty Cash Vouchers	Cash Book Postings	Dr.	Cr.	Bought Ledger Cash Postings	Day Book Postings and Additions	Invoice Book Postings Additions	Returns Books Postings and Additions	Journal Entries Examined and Postings	Statements for Payments	Stock Account	Bought Ledger Balances	Sold Ledger Balances	Trial Balance agreed	Private Ledger written up	Balance Sheet & Profit & Loss A/c completed	Remarks
1902																					
January ..																					
February ..																					
March ..																					
April ..																					
May ..																					
June ..																					
July ..																					
August ..																					
September ..																					
October ..																					
November ..																					
December ..																					
1903																					
January ..																					
February ..																					
March ..																					
April ..																					
May ..																					
June ..																					
July ..																					
August ..																					
September ..																					
October ..																					
November ..																					
December ..																					

.....& Co.

It will be seen that the above differs from the specimens already described in much the same manner as a Ledger differs from a Journal. Instead of a separate book being employed for each audit, a folio of the Audit Note-Book is devoted to that purpose, and it will further be seen that the specimen ruling shown provides for a monthly audit extending over two years.

As this is an office book, rather than a portable one, it is written up from memorandum books, one of which is devoted to each audit, or it may be written up from the diaries of the audit clerks. In any case, however, it would seem that some sort of Audit Note-Book would require to be kept for each separate matter, in which memoranda and queries might be recorded; but it will be obvious that if the audits are fairly uniform in character, the information afforded by the above book would be of the greatest convenience to principals in supervising the work of their various audit clerks, and generally ascertaining the state of the various matters in hand.

THE OBJECT AND SCOPE OF AN AUDIT.—The next point to be considered is the object and extent of an audit. The object of an audit may be said to be threefold:—

- (1) THE DETECTION OF FRAUD.
- (2) THE DETECTION OF TECHNICAL ERRORS.
- (3) THE DETECTION OF ERRORS OF PRINCIPLE.

On account of its intrinsic importance the detection of fraud is clearly entitled to be considered an “object” in itself, although it will be obvious that it can only be concealed by the commission of a technical error, or of an error of principle. It will be appropriate, therefore, to combine the search after fraud with search for technical and fundamental errors; but it can never be too strongly insisted that the auditor *may* find fraud concealed under *any* item that he is called upon to verify. His research for fraud should therefore be unwearying and constant.

It has been asserted by some that the whole duty of the Auditor is to ascertain the exact state of his client's affairs upon a certain given date. This is, in effect, the same thing as saying that he is only responsible for the correctness of the Balance Sheet. Even if this be the case—and it is open to considerable doubt, as the extent of an Auditor's duties depends entirely upon the terms of the express or implied contract between himself and his client—the Balance Sheet cannot well be verified without a proper examination of the Revenue Account, which in its turn involves a complete examination of the books.

The detection of fraud is a most important portion of the Auditor's duties, and there will be no disputing the contention that the Auditor who is able to detect fraud is—other things being equal—a better man than the Auditor who cannot. Auditors should therefore assiduously cultivate this branch of their functions—doubtless the opportunity will not for long be wanting—as it is undoubtedly a branch that their clients will most generally appreciate.

Before dealing with the various methods to be adopted to ensure the detection of errors, it will perhaps be not out of place to enquire what is the *extent* to which an Auditor is expected to carry his research. This will naturally vary according to the circumstances of each individual case; but, even allowing for this, the greatest diversity of opinion obtains, some claiming that an Auditor's duty is confined to a comparison of the Balance Sheet with the books, while others assert that it is the Auditor's duty to trace every transaction back to its first source. Between these two extremes every shade of opinion may be found; and, among others, the opinion of most practical men. Were the Auditor's functions limited to a certification that the Balance Sheet submitted to him was in accordance with the books, it would be difficult to conceive why the old-world amateur Auditor should have been found so lamentably wanting; on the other hand, it cannot be denied that (except in concerns of comparative insignificance)

a minute scrutiny of *every* item would be quite impossible to the Auditor—nor indeed is such a detailed audit often necessary, although it is in the highest degree desirable that every undertaking should possess the means of enabling the *staff* to make such an examination for itself.

Upon this subject the opinion of the late Mr. JOSEPH SLOCOMBE, F.C.A., will be found valuable. "There are some cases," said Mr. SLOCOMBE, "wherein an audit, to be efficient, should comprehend an examination of every entry in the books; there are others—more numerous—wherein the accuracy of the accounts may be verified by tests which render the checking of every posting unnecessary. Speaking generally, the Cash Book, which is in truth the root and foundation of all, should be exhaustively examined, both as to receipts and payments, and checked into the Ledgers and other books of account under review. The whole of the postings of the Nominal and Private Ledgers should also be checked, and the nature of the entries in them scrutinised." This is, probably, as much as can be said upon the subject generally, but it raises two points which claim attention before proceeding further.

The "tests" spoken of by Mr. SLOCOMBE clearly include some sort of system by which each Ledger may be separately balanced, and its correctness thereby (presumably) verified. This is a matter that will be dealt with at some length later on, and its further consideration may be postponed until that time.

The second point is of great importance. It is in the highest degree necessary that the Auditor, before commencing his investigation, should thoroughly acquaint himself with the general system upon which the books have been kept. It is very usual for the Auditor to be supplied with a list of the books in use (by Section 7 of 42 & 43 Vict. c. 76, this is compulsory in the case of Banking Companies registered under the Act, and a similar provision is contained in the articles of association of many companies), and such a practice is, indeed, very desirable. But it cannot be too strongly insisted that such a list can only be of any real utility when the Auditor thoroughly

grasps the uses, and the possible abuses, of which each book is capable. Numerous instances have been known of an audit entirely failing through neglect in this respect.

Having thoroughly made himself master of the general system of accounts in use, the Auditor should look for its weakest points, "Where is fraud most likely to creep in?" he should ask himself; and, if he can find a loop-hole, let him be doubly vigilant there. But never let him for a moment suppose that, because he sees no opportunity for fraud, none can exist. To the intelligent Auditor who has grasped his system thoroughly, it is generally practicable to dispense with *some* portion of the mechanical means of checking. To what extent this can be done with safety must always remain a question for each Auditor's own intelligence and experience to answer, and it may be added that probably he must take the risk of any consequences that may ensue; but—so far as the matter can be dealt with in a general treatise—its solution will be sought after in these pages.

Before leaving this subject, it may, perhaps, be well to add that, under the expression, "mastery of the general system," perusal of the deed of partnership, memorandum and articles of association and registered contracts, deed of settlement, special Act of Parliament, and any and all other documents that, *per se*, affect the general constitution of the concern, are included.

ADVANTAGES OF AN AUDIT.—The question has been raised from time to time as to what advantages may be reasonably expected from a proper professional audit of accounts. In addition to those mentioned in the preceding paragraph, as coming under the head of the primary objects of auditing, it may be pointed out that the proprietor or proprietors of a business will not only have the advantages of having placed before them an accurate statement of their affairs, together with a Profit and Loss Account showing how this position has been arrived at; but that they would also have available certified accounts as to profits which cannot fail

to be of the greatest convenience, either in the event of their wishing to sell the business to a private trader, or firm, or to a limited company, or in the event of one of the partners dying or wishing to retire. Under each of these circumstances the importance of a thoroughly reliable statement of profits cannot well be over-estimated, and the convenience it affords—as well as the enhanced price which can be obtained in the event of a sale—will under all normal circumstances more than compensate for any slight expense which the audit may have originally involved. So far as private firms are concerned, an efficient audit possesses the further advantage that, by reason of its ensuring a periodical preparation of reliable accounts, it tends to minimise the risk of partnership disputes, with all their attendant annoyance and expense. Accurate accounts are also valuable as preventing an over-assessment for Income Tax or enabling Tax over-paid in error to be more easily recovered: these are also of the greatest possible value to both sides in compensation cases.

In the case of companies the audit assumes a slightly different application owing to the special nature of the contract and to the statutory regulations affecting the matter. The company Auditor is not expected to act as the financial adviser of the undertaking—a position that is frequently thrust upon him in connection with private audits—his duty being rather that of an Auditor appointed in the interests of a sleeping partner. It devolves upon him to examine the accounts of their stewardship, prepared by the active partners—*i.e.*, the directors—and to state whether in his opinion those accounts are correct, and fully and fairly disclose the position of affairs, or in what respects they fail to do so.

In addition, it may be pointed out that various cases reported in Appendix “B” to the present work show that in the event of an Auditor, through his negligence, failing to discover fraud or embezzlement on the part of the employees of the client, he may be held liable in damages for the amount lost as a result of his negligence. This liability involves, of course, a

corresponding benefit to the persons in whose favour the liability accrues, and is consequently a factor that ought not to be lost sight of in weighing the advantages of an audit. It is, however, perhaps hardly necessary to add that the Auditor does *not* insure the honesty of his client's employees.

In an address to the Manchester Chartered Accountants Students' Society (*vide Accountant*, 22nd February, 1902) Mr. ERNEST CREWDSON, F.C.A., has expressed dissent from these views, and pointed out that the duty of an Auditor is merely to "stand between the shareholders and the board." Were this definition to be accepted, it would follow that there could not be such a thing as an audit apart from a joint-stock company, whereas Auditors are, of course, of far older origin than companies are (*vide* Appendix "C"). The duties of company Auditors are, however, in some respects of a special character, being—at all events, in part—defined by statute. Such legislation as exists must, of course, be respected, and in practice the protection it affords may prove useful; but it must never be forgotten that there is a broad distinction between the legal limit of pecuniary responsibility, as defined by the law, and the reasonable requirements of a high standard of professional efficiency. These points are more fully considered in Chapters IX. and X.

METHOD OF AUDIT.—A comparison of the relative merits and disadvantages of CONTINUOUS AND PERIODICAL AUDITS is worthy of more attention than it has attracted in some quarters.

THE CONTINUOUS AUDIT sometimes includes the preparation of the periodical accounts by the Auditor's staff. Its advantages may be said to be : (1) The examination occurs sooner, and consequently any errors committed are more quickly detected and rectified; (2) the periodical visits of the Auditor keep the bookkeeper closer up to his work; (3) a more detailed audit is practicable; (4) the audit can be completed soon after the closing of the books, without unduly hurrying

the examination. On the other hand, there is always a danger of items that have been checked by the Auditor being altered (either ignorantly or fraudulently) before the final audit; and it is therefore necessary that the clerk in charge of a continuous audit be very wide awake, and have a very clear idea of the system under which he is working.

It has been found a good plan to adopt a special "tick" for the verification of all figures upon which a correction appears, as, if this plan is adopted, a correction made after the tick has been affixed will be more readily discovered. It goes without saying that the difference in the two ticks should be as slight as possible, and the bookkeeper should *not* be told what the difference implies.

THE PERIODICAL AUDIT (by which is meant the audit begun after the periodical accounts have been completed) obviates this difficulty to a certain extent, and, if the books remain in the Auditor's sole custody during the duration of the audit, entirely; but the drawbacks it presents (which are, naturally, the advantages of the continuous audit) render its adoption impracticable, except in small concerns or in partial audits, unless the books can be so arranged that very little detailed checking has to be done by the Auditor.

The risks involved in leaving the books in the hands of the bookkeeper during the audit are undoubtedly very considerable; but, so long as these difficulties are not lost sight of, there is but little doubt that common sense and a general alertness will save the Auditor from this—as well as many another—danger. Moreover, where the Auditor himself closes the books—and this will not infrequently be the case in small audits conducted continuously—it should be difficult for fraud on the part of the staff to altogether escape detection.

It would be well to mention here the extreme importance of *completing* each item of the audit as soon as possible after it is begun. Extensive frauds have escaped detection because the Auditor checked the balances of a Ledger one day, and the additions of such balances on the next—some of the items

having been altered in the meantime. It will be obvious that had the additions been checked on the same day as the extraction of the balances, and a note taken of the total, the fraud would have been impossible.

What may be described as the "ideal" audit is one combining the two modes of investigation just described. It is sometimes attained by the employment of two independent Auditors, one performing a continuous and the other a periodical audit; but more frequently the continuous audit is done by "staff" Auditors, or by the client's ordinary employees under a good system of internal check. In the case of companies registered under the Companies Acts, the Auditor has "a right of access *at all times* to the books and accounts and vouchers of the company": this right would appear to involve a corresponding duty in all cases where such a course seems necessary in the interests of the company.

CALLING BACK POSTINGS.—Having now cleared the ground of various preliminary considerations, the manifold points arising in the course of an ordinary audit will be dealt with.

It has been seen that in every instance it will be necessary for at least some of the postings to be called over; and inasmuch as by that means the Auditor will at once acquaint himself with the nature of the transactions that have occurred, the calling back of such postings will form an appropriate starting-point for examination. Many persons prefer to start with an examination of the Vouchers, and, if the Vouchers are rich in detail, it will frequently be desirable to take them first; but when—as is often the case—they are mostly bare receipts for so much money, it will generally be best to start with the postings.

It is well to commence with the posting of the Cash Book, even when all the postings are to be checked, as by this means a general idea of the business done is most quickly grasped; which is very desirable. The calling over of postings can hardly

be too carefully done, and although the work is decidedly mechanical—and, consequently, somewhat somniferous—it must be most conscientiously performed. In particular, care must be taken not to pass any item already ticked, unless it be certain that it has inadvertently been ticked in the regular course of audit; and also any items remaining unticked after the calling over is completed should receive most careful attention. Inexperienced clerks are apt to “suppose” they ought to have ticked an item, or to “suppose” they ticked such-a-one instead of such-another. Either “supposition” may cause a fraud to remain undetected, or (which will, perhaps, appeal to the youthful mind more powerfully) may keep him late at his work night after night, while the senior audit clerk hunts up and down for an error in the Trial Balance. When the error is discovered to be a mistake in the posting that was passed in calling back, it is possible that the unfortunate junior will be even more sorry that he ever ventured to “suppose.”

Where it is intended to check every posting, it is a good plan, after the cash postings have been checked, for the remaining postings to be called back from the Ledger into the Day Books, &c.; and it will probably save time, while going through the Ledgers, to check the additions and balances at the same time, and so finish each Ledger at a sitting. This method, however, is not always convenient, or even possible, and much must therefore be left to the discretion of the clerk in charge.

BAD OR AMBIGUOUS FIGURES should always receive close attention, as it not infrequently happens that they are posted as one figure and added up as another. Corrections, too, require careful attention. Erasures should always be strictly prohibited; and where hand-made paper is used for the books, they should be keenly watched for, as a clean erasure may easily have been made. It is very important that the room used by the Auditors be well lit, or mistakes may easily occur. Where a correction has been made, care must be taken to insure that the addition and posting have both been altered.

In a continuous audit this is especially important, but—as it has already been noticed—it need not now be dilated on.

It may seem almost superfluous to say that the clerk calling back should always speak clearly, but experience teaches that this is a matter that frequently does not receive the consideration it deserves. Such a mistake as £20 3s. 9d. being posted £23 9s. od. may be guarded against by emphasising the last syllable of the pounds, thus—“Twen-ty, three, nine.” It is important that the clerk calling should learn to “pull with” the one who is turning over folios. This is a habit much more readily acquired by some juniors than others—in many respects it resembles the art of accompanying in music—and the senior who has found a youngster to suit him will not willingly make a change, as the economy of nervous force consequent upon perfect accord is very considerable.

CHECKING ADDITIONS.—In all cases it is desirable, although it is not always practicable, that all the additions should be checked. In every case, however, the additions of the Private Ledger, Nominal Ledger, Cash Book, Bill Books, Petty Cash Book, and Wages Book will require to be verified. This should always be done when the other work connected with the same book is being done; for if the bookkeeper has power to make alterations meanwhile, he can afford to laugh at every safeguard against fraud.

It is hardly necessary to add that the checking of additions, though purely mechanical, is most important work. It is especially necessary that the “carried forwards” be checked on to the following page, as errors frequently occur here. Also, when checking the additions of a book with several columns of figures, it is important to see that the distinction between the various columns is preserved when carrying forward totals from one page to another.

THE PREVIOUS BALANCE SHEETS.—While the junior clerk is checking additions, the senior will have time to see to many matters which require his attention. Foremost among these will be the comparison of the Ledgers with the

last Balance Sheet—unless, indeed, the principal has already dealt with this point.

It is very generally conceded that no Auditor can be made liable for the acts or omissions of his predecessor in office; but this rule must, of course, be strictly applied, and an Auditor who adopts and perpetuates the mistakes of his predecessor would not on this account alone escape the consequences of his own negligence. It is important, therefore, to carefully scrutinise those items which, in the ordinary course, are brought forward as balances from one year to another. In so far as their correctness cannot be tested by an examination of the accounts under review, the present Auditor is, doubtless, not responsible; but in cases where a careful investigation of the current accounts would have disclosed an error in the previous accounts, it might well be held that the discovery ought to have been made, and that failure to make it was the result of negligence. It is not thought necessary to pursue this subject in detail. It may be pointed out, however, that the mere existence of a Ledger Account headed "Reserve Fund," with a balance to the credit thereof, should not be taken as conclusive evidence that a corresponding amount of profits available for distribution has been transferred to Reserve; while it would be only prudent to see that proper Depreciation had been written off all wasting assets in prior years, as well as in the year under review.

It need, perhaps, hardly be added that it is important that the Auditor should see that he begins his investigation at the exact point where the previous investigation left off—that is to say, the opening balances of the period under review should in all cases be checked and agreed with the previous Balance Sheet. This applies whether or not the accounts for the previous period were checked by the same Auditors. Under normal circumstances this checking of the opening balances would probably be done as a matter of course, but the question as to its necessity might sometimes arise where it is the custom to start an entirely new set of books with each financial year—more especially if the auditing is done at the Accountant's

office, and not at the client's place of business. By way of showing the extreme importance of adopting this somewhat obvious precaution, it may be added that, some few years since, a case of somewhat extensive fraud transpired, extending over a long period, which might have been discovered at any time, had the Auditors checked the starting balances with the previous year's books.

VOUCHERS.—Much might be written, and, indeed, has been written, upon the important subject of Vouchers: it is however, impossible to treat the matter exhaustively in the space at disposal. A paper by Mr. HOWARD S. SMITH, F.C.A., upon the subject was reproduced in *The Accountant* of 14th January 1888, which may be consulted with advantage. An interesting essay on the subject (by Mr. LESLIE STEDMAN, A.C.A.) also appeared in *The Accountant* of 25th January 1902. Much useful information of the detailed work of vouching will be found in "A Municipal Internal Audit," by Mr. ARTHUR COLLINS.

The present work would, however, be incomplete without some mention of the matter, which, for convenience sake, will be dealt with under the following heads :—

- (a) Receipts.
- (b) General Payments.
- (c) Petty Cash.
- (d) Wages.
- (e) Bank Account, &c.
- (f) Journal Entries, &c.

Each of these involves, for its complete consideration, the question as to the form of accounts employed, but the relative merits of the various forms available will mostly be more conveniently dealt with at a later period. In general terms it may be mentioned that the process of "vouching" consists of obtaining *evidence* (usually documentary) that the transactions recorded in the books are *facts*.

(a) RECEIPTS.—It is part of the Auditor's duty to ascertain, as far as possible, that all cash received has been entered to

the debit of the Cash Book. The usual mode of verification available will be a comparison of the counterfoils of the Receipt Books with the Cash Book entries. Counterfoils should always be numbered, and the bookkeeper should mark the Cash Book entry with the number of the receipt. It is necessary that the Auditor should notice that the numbers of the counterfoils run consecutively, and if there are any numbers missing, or any counterfoils left blank, a satisfactory explanation must be found. If a receipt has been cancelled, the body should remain attached to the counterfoil ; for it need hardly be pointed out that this is much more satisfactory than any other explanation possible. The receipt for two accounts paid together should be acknowledged on two separate forms. If there be no hard and fast rule, there is nothing to prevent the collector from using separate counterfoils while only using one receipt, which, of course, leaves him an extra receipt form to use for another acknowledgment which he need not account for. Defalcations have frequently arisen, or remained undetected, from a neglect of this precaution.

On the other hand, there are some cases where it may prove better to *forbid* the use of two receipts for two payments made the same day. This course, however, leaves it open to the collector to account for the two payments on different days, and so gain possession of a blank form. In either case, the special point is that there should be one fixed rule, which should be rigidly maintained. But, whatever precautions be taken, the method is by no means infallible, and in consequence many Accountants have advocated the issue of a circular to all customers, requesting a verification of their respective accounts as quoted. This method is, of course, quite impracticable with a retail business, but among wholesale houses would probably prove a valuable precaution. As a rule, however, wholesale accounts are run upon certain known terms as to credit, so that any irregularity would be apparent to the observant Auditor. In any case, the Auditor must not communicate with his client's customers on his own responsibility ; and, as a rule, the practice is thought undesirable,

save in cases of grave irregularity, when some special enquiry becomes absolutely necessary in order to ascertain the actual position. It need hardly be added that the mere statement by a customer that he has paid his account cannot always be regarded as conclusive.

It has, unfortunately, become the custom of many large firms to send their own form of receipt with remittances, and the efficacy of counterfoil Receipt Books is thereby much impaired. So far as possible, the Auditor should ascertain what firms do adopt this practice—and here he will, perhaps, find the knowledge gained at one audit may help him to detect something wrong at another.

Dividends and compositions in Bankruptcies, &c., will inevitably have been accompanied by a special form of receipt; if, therefore, such entries be found upon a receipt counterfoil, the circumstances may well give rise to suspicion. The counterfoil of the dividend notice should always be produced as a voucher.

The dates of the counterfoils should always be compared with the Cash Book entries.

Cash Sales require very careful scrutiny, and the method of internal check adopted should always be ascertained, and, as far as possible, perfected. Where practicable, it is most desirable that the clerk who writes up the Cash Book should not be the one who receives the money.

Special items of receipt will be more conveniently dealt with when considering the audit of various kinds of accounts.

(b) GENERAL PAYMENTS, other than those for wages and petty cash, should (where possible) be invariably made by cheque, payable to "order," and crossed. Even where the amount is only a few shillings this method of payment will, in the vast majority of cases, be simpler, as well as safer, than cash payments. Such payments by cheque hardly require vouching, but it should nevertheless be done, nor will the process be difficult. Receipts can readily be obtained for all ordinary pay-

ments, which should be numbered consecutively (the numbers of the cheques are very useful for this purpose sometimes), as should also the items in the Cash Book.

A receipt on the payee's own printed form is very much better evidence that he has received the amount stated, than a receipt on the form of the payer, although, doubtless, a uniform style of voucher will save the Auditor's time slightly. From both points of view, it is not desirable that *payers* should provide their own form of receipt; be this as it may, however, the practice exists, and will probably continue to do so.

Some special payments cannot be vouched in the usual way (*e.g.*, insurance premiums on a new policy), but satisfactory evidence that the payment was actually made, and value received, should always be obtained. An Auditor whose practice is mostly in one particular industry will soon get to know the signatures of most trade houses; and, doubtless, this knowledge might often prove valuable; for, although any clerk is frequently deputed to acknowledge receipts, yet the endorsement of the cheques will usually be done by one hand alone.

(c) PETTY CASH.—Whatever system of petty cash be adopted, the vouching of petty cash, as a whole, will be the only possible real verification of the payments made from cash to petty cash, and the whole matter may be appropriately considered here. The actual inspection of petty cash vouchers may, or may not, be undertaken by the Auditor, as he thinks fit. In the former case, a responsible person must certify the whole of the items *en bloc*; and in the latter case, a similar person must pass each separate voucher. Important frauds are hardly likely to occur in petty cash; but, as likely as not, petty peculations will arise, if an efficient supervision be not exercised. No Auditor can properly supervise the petty cashier, and it is well to acknowledge the fact fully; he may, however, see that every payment has been duly authorised by the responsible head, that the payments made by the cashier have been duly acknowledged, that the additions of the Petty Cash Book are correct,

and that the balance unspent is in hand. Beyond this he should not attempt to go.

Some clients have a very bad habit of making comparatively large payments through petty cash. This should be discouraged as far as possible. Some have a still worse habit of allowing the petty cashier to *receive* small amounts: this is a very bad system, and should be most vigorously contested. All receipts should be banked, no matter how trifling in amount, and a clerk in charge of cash receipts should never be in charge of cash payments.

(d) WAGES.—Instances of fraud in the payment of wages are among the most frequent of those that come under the notice of an Auditor; but, from the very nature of the case, direct evidence of proper payment is all but impossible. Signatures might, and frequently are, required from each man receiving wages; but some men can only sign by means of affixing their “mark,” while many others would not be above “going shares” with the paying clerk in anything they could get over their due. Circumstantial evidence is thus the best available for the Auditor, and this will consist in a good *system* of payment, which renders fraud improbable by reason of the number of persons concerned in the preparation of the pay-sheet and the subsequent payment. Particulars of time worked, or piece-work done, should be certified by the foremen; the calculations of wages worked by one office clerk, and checked by another; the cash for the wages made up by the cashier, and the wages paid by him or his deputy in the presence of a works manager. Where possible, a cheque should always be drawn for the exact amount of wages required. The Auditor should inquire as to the particular system adopted, and should ascertain that it is really carried out; sometimes it might be well for him to unexpectedly put in an appearance when the wages are being paid. The Wages Book should always be added, and a week or two’s wages should be taken at random, and checked up and down.

A case of some interest to Auditors, in connection with frauds in wages was tried before Mr. Justice JELF in the Liverpool Assize Court in December 1902. The evidence showed that these frauds had been going on for upwards of sixteen months, and that during that time sums of money, amounting in some weeks to over £70, were stolen from the Mersey Docks and Harbour Board by means of bogus Wages Tickets, which were brought into existence by the prisoner LYNCH. The total wages in the Engineers' Department, in which the frauds were committed, usually amounted to upwards of £10,000 per week, and in the sixteen months £3,200 was stolen. The prisoner LYNCH was a time-keeper, whose duty it was to enter up the time worked by the various men in his district in a Time Book kept by him. The prisoner ROUS was a ticket clerk, whose duty it was to attend every Saturday on the payment of wages to the men in the district to which LYNCH was sent in the first period, to give out the Wages Tickets. During the first period LYNCH's men received their wages at No. 2 pay-station, where ROUS was ticket clerk. The men were divided into two classes, "permanent" and "extra"—the latter being taken on for temporary jobs, and therefore not going through the Board's books in the same way as the permanent men. It was by using the names of fictitious "extra" men that LYNCH perpetrated the frauds. As time-keeper it was his duty to take the time of the men in order to provide a check on the Time Sheets sent in by them, and in order that the necessary provision might be made for the payment of wages (which were always paid one week late), it was his duty, towards the end of the current week, to go to the Time Office and dictate to a time-bookkeeper the names, time worked, and the rate of wages of the various men whose times he had so taken, and this dictating of the names was the only step in the Board's system of internal check that was not automatic. The especial importance of this point arises from the fact that frauds may naturally be expected to occur at the weakest point in any system. LYNCH's plan was to dictate bogus entries, along with genuine ones, to the time-bookkeeper, who (having no precise knowledge of the facts) naturally entered whatever particulars

were dictated to him. On Mondays the Time Book was sent to the Wages Bill Office in order that Wages Tickets might be prepared there in accordance with the Liverpool Time Book. In due course these tickets and wages were provided week by week for all names contained in the Time Book. It was LYNCH's duty to send to the Engineer Time Sheets certified by him as correct. These were entered up by him from his Time Book so as to include the bogus as well as the genuine names. ROUS, as ticket clerk at the No. 2 pay-station, ought to have given tickets only to workmen who claimed them; but in point of fact he enabled LYNCH to get possession of the Wages Tickets made out in respect of the bogus names, and LYNCH having obtained possession of these tickets secured payment of corresponding sums as wages by sending various persons to cash them at the pay-hut. In April 1902 LYNCH was transferred to the Dockyard, while ROUS remained as ticket clerk at the No. 2 pay-station. This circumstance draws attention to the advantage of occasionally varying the duties of employees, as apparently with the transference of LYNCH these particular frauds ceased altogether. LYNCH thereupon appears to have cast about for a new method of falsification. In his new district there were no "extra" men employed, and his former system was therefore inapplicable. He accordingly took the names of men on sick leave, or of men who had only recently left the Board's employ, which names were, of course, familiar to the bookkeeper, and therefore in the absence of any direct system of check aroused no suspicion. Till August 1902 he appears to have resorted to various methods of wages payments in use by the Board, *e.g.*, for reissuing tickets not claimed or for issuing tickets and paying wages on Friday nights. To effect these frauds he was obliged to resort to forging or altering various documents used by the authorities for the issuing of tickets and the payment of wages. Both prisoners pleaded guilty, and LYNCH was sentenced to seven years' penal servitude, while ROUS, who was merely his accomplice, escaped with a more lenient punishment of six months' imprisonment, with hard labour. The case is of especial interest, partly on account of the

length of time that the frauds remained undiscovered, and partly because the system of internal check in force was regarded as being completely adequate. The above particulars, however, will show sufficiently clearly exactly where the system broke down in practice.

(e) BANK ACCOUNT, &c.—All payments into the Bank should be checked off against the Pass Book. The composition of a few such payments (as shown by the counterfoil paying-in book) may be advantageously compared with the items which they purport to represent, and any irregularity carefully followed up. The credit side of the Cash Book should also be checked off against the Pass Book, and any disagreement of the *names* should receive careful attention. The Bank Balance must, of course, be verified, and if the Auditor has not himself received the Pass Book from the Bank, he should make a point of either obtaining the Bank's certificate as to the balance standing on the date of the account, or take it back to the Bank, in *person*; otherwise he will run the risk of never having seen the *real* Pass Book at all. If there be a balance of cash in hand it must be verified, and the Auditor should ascertain that it has not been made good by means of a cheque *drawn since the books were closed*.

In a continuous audit, the vouching should always be kept as close up to date as possible, while the Bank and (*all*) Cash Balances should be verified at every visit. A Cash Balance will sometimes be found to consist largely of "I O U's"; this should always be discouraged as far as possible, and it may be necessary to call the attention of the chief to its undesirable preponderance. In any event, the "I O U's" should be initialled by someone in authority.

(f) JOURNAL ENTRIES, &c.—The modern Journal being the book of first entry in which comparatively unusual transactions are recorded, it becomes just as important that the Journal entries should be fully vouched as it is that those relating to cash receipts and payments should be subjected to the same

scrutiny. If the correctness of all entries passed through the Journal be taken for granted, there is absolutely no limit to the amount of falsification that might be committed with impunity. Improper Journal entries might be made with one of two objects—namely, (1) to conceal defalcations, as, for instance, when customers are improperly credited with the amount embezzled, and a corresponding debit made to Allowance or Bad Debts; (2) to fraudulently exaggerate the profits of the undertaking—*c.g.*, by crediting nominal accounts and debiting real accounts with payments that cannot properly be capitalised. It is impossible to deal in detail with the vouching of Journal entries, on account of the very various nature of the transactions that might be recorded in this book; it may be stated, however, that only the evidence of some disinterested party—or, that being obtainable, the evidence of some person absolutely above suspicion—should be accepted as a voucher, and in the case of all important entries the Auditor should take steps which will enable him to form a definite opinion of *his own* with regard to the matter.

A practical consideration in connection with vouching is with regard to the actual marks an Auditor should make to indicate that this work has been performed. In the first place, the voucher should be so marked that it cannot be afterwards used as a voucher in support of another entry; and, in the second place, the entry that has been vouched should be so marked that the Auditor can afterwards readily ascertain what items remain unvouched. With regard to the marking of the vouchers, the following methods are in use:—

- (1) A large “tick” across the face of the voucher.
- (2) The Audit Clerk’s initials.
- (3) A rubber stamp bearing the name of the firm—either with or without the clerk’s initials.

As the main object is to so disfigure the voucher that it cannot be again used in support of another entry, it is not very material

which of these three be employed. It may be remarked, however, that initials necessarily take longer to make than a tick or an impression from a rubber stamp. The first method is, it is thought, generally preferred; but where two firms of accountants are joint Auditors, the use of a rubber stamp is desirable, as indicating clearly who is responsible for the cancellation. In other cases the record in the Audit Note-Book ought to be sufficient for this particular purpose. With regard to the marking of the entries in the books as being vouched, some firms employ a distinct "V," which has the advantage of being clearly distinguished among various classes of ticks, and so enabling a list of missing vouchers to be more readily compiled. Sometimes, however, an imperfect voucher is accepted, and in such case it seems desirable that a special form of mark should be employed, so as to guard against the real voucher being produced in support of another entry. Many firms, therefore, employ the following marks by way of a "cross-tick" against the ordinary posting tick:—

Where a regular voucher has been produced



Where the only voucher is an endorsed cheque



Where payment was made on a bearer cheque,
but the entry has been traced to the credit
side of the Bank Pass Book



Where the Auditor suspects irregularities that he is unable actually to detect, he may frequently gain his point by *feigning laxity* in his method of vouching; this will often serve to induce that carelessness on the part of the defaulter that is necessary for his detection and exposure. The author, who has had a considerable experience of frauds of all kinds, has found this method work admirably; it is, however, necessary that it be practised with discretion, if one wishes to avoid the charge of being actually lax.

BILLS OF EXCHANGE.—A few words on the subject of Bills will not be out of place.

BILLS PAYABLE will present but little difficulty; the returned Draft forms, of course, the voucher for the payment of Bills matured, while the Bills running (as shown by the Bills Payable Book) will explain the balance of the Bills Payable Account in the Ledger.

BILLS RECEIVABLE require more careful consideration. The Bills Receivable Book should be dealt with *seriatim*; all Bills matured or discounted should be traced into the Cash Book, and, if dishonoured, back to the debit of the customer. All Bills dishonoured, or still running and undiscounted, should be in hand, and this fact must be verified.

Discount deducted from Bills discounted should be looked into to a certain extent, although not necessarily exhaustively; also, the important questions of the liability upon Bills under discount, and the value of Bills dishonoured, must not be lost sight of. Both these points require to be considered when the provision for bad and doubtful debts is dealt with.

Dishonoured Bills should never be allowed to remain on the Bills Receivable Account of the Ledger.

✧ **CONSIGNMENTS.**—It is very desirable that all points connected with consignments be checked up and down as much as possible; and for this purpose letter-files, copy letter-books, and accounts current should be freely consulted. There is, however, nothing particular in the nature of the transactions (save the question of foreign currency, which is dealt with elsewhere) that calls for special comment here.

THE TRIAL BALANCE.—It should be the Auditor's aim so far as possible, to carry each department of his investigation right up to the Trial Balance at the same sitting. Of course, in an important audit, this can very rarely be accomplished; but the Auditor must always remember that there is material danger in leaving any portion unfinished in the hands of bookkeepers or cashiers, who—for all he can know to the contrary—may manipulate the figures during the course of the audit. The

Auditor, therefore, should endeavour to fix everything up as he goes along, and where he cannot finish the same day, he will do well to keep possession of the books and documents until he can. In fact, he should, so far as possible, keep everything in his own hands until the audit is completed as far as the Trial Balance. Having once secured a Trial Balance that he knows has not been tampered with, the Auditor may cease to trouble himself about the materials from which it was built up—they may be manipulated and altered up and down, but he holds in his own hand the key of the whole position. Nor need the course indicated cause offence, or even excite suspicion, if carried out with tact. It is generally an easy matter to hang on to a list of balances, and not often difficult to “take home” a book so as to get it finished. And, even where this cannot be accomplished unostentatiously, a few notes and private marks will often serve the purpose. It is not a difficult matter to acquire a “tick,” which, while looking much the same as any other, can be instantly distinguished from a forgery. A man forging ticks will be much less careful as to their form than a man forging initials, and can thus be more often detected. It is not a bad plan to carry about one’s own coloured ink, and to take care that it is a different make from that in general use at the offices where the audit is conducted. The Auditor, however, must be careful not to talk about these things; and he should also be careful not to leave his ink about. It is often a great advantage to employ ink of a different colour to that used at the preceding audit.

BALANCING.—In the foregoing paragraph it has been assumed that an exact balance has been arrived at by the book-keepers before the Auditor commences his investigation. This, of course, is as it should be, for clearly it is no part of the Auditor’s duties (as such) to balance the books. The question arises, however, as to whether an Auditor is ever justified in passing accounts that do not exactly balance. Obviously, accounts that do not balance cannot, in the nature of things, be entirely accurate; but so long as the Auditor is satisfied that the discrepancy arises from one error, and not from the combined

effect of numerous errors, and so long as the difference is so small as to have no practical effect upon the ultimate result, the absence of an accurate balance may sometimes be disregarded. Here, as elsewhere, however, much depends upon circumstances: a Nominal or Private Ledger—or, indeed, any Ledger with less than, say, 500 accounts—ought certainly to balance exactly; on the other hand, it is hardly practicable to ensure an absolute balance with a large Trade Ledger—hence the importance of these balances being tested at frequent intervals, say monthly at least.

METHODS OF BALANCING.—In private audits it not infrequently happens that the Auditor is requested to balance the books. The detection of errors in balancing is thus a matter with which an Auditor occasionally has to deal, although it does not in any sense form part of the actual audit itself.

There are two modes of seeking for errors in balancing:—

- I. By localising the error.
- II. By tabulating the Ledger Accounts.

LOCALISING THE ERROR.—This is, of course, best accomplished by framing the system of accounts upon such lines that each separate Ledger is “self-balancing.” Where this has been done, it is a very simple matter to see in which Ledger or Ledgers the discrepancy arises, and the field is at once narrowed accordingly. It may easily happen, however, that the various Ledgers have not been framed upon self-balancing principles; even then it does not necessarily follow that the error cannot be localised. If the Cash Book be in tabular form, or if there be separate subsidiary Cash Books, the equivalent of an Adjustment Account can almost always be constructed; transfers from one Ledger to another may complicate matters, but unless such transfers are much more numerous than is usual, they will hardly present any very serious difficulty. On the other hand, it is not often practicable to apply this method if it necessitates an analysis of the Cash Book.

When the books of first entry have not been in the first instance so formulated as to readily lend themselves to the construction of self-balancing Ledgers, a method of check described by Sir J. G. CRAGGS, F.C.A., in his "Heavy Trial Balances made Easy," will be found of considerable value. A complete description of this system would be impracticable here; but it may be mentioned shortly that the system consists in requiring the clerk calling back from the book of first entry to the Ledger to compile, *as he calls back the various entries*, a list of the amounts posted into each separate Ledger. By this means the total amount posted into each separate Ledger, and the sources from which it is posted, may be readily ascertained. The system also provides a convenient means of quickly discovering any clerical errors that may have been made in the compilation of the abstracts. Where a large set of books has to be balanced for a comparatively long period this system will be found most useful, the more so because—so far from adding to the time required for calling back the postings—it utilises the time of the junior which would otherwise be wasted, and thus directly tends towards both accurate and expeditious work. It need, however, perhaps hardly be added that those who contemplate attempting this method for the first time should not do so before thoroughly mastering all its details, as explained in the handbook referred to.

TABULATING THE LEDGERS.—This is a method which is sometimes adopted where the number of Ledger Accounts is not large, and, where practicable, it is extremely thorough. It consists of making an abstract of every Ledger Account upon sheets, which are virtually Tabular Ledgers. When the abstract has been completed, the checking of the cross-additions proves the extraction of the Ledger balances, while a comparison of the longitudinal totals with the opening balances, Day Book totals, total of Cash received, &c., will show in which direction the error lies. Thus, if the total "Goods Sold" does not agree with the total "Sales Account" in the Nominal Ledger, there is clearly an error in the postings or the additions of the Day

Books. Many accountants, however, and among them the author, prefer to carefully re-check the Ledger, item for item, rather than adopt such a laborious process of localising the error—especially when it is remembered that even when the abstraction of the Ledger has been completed, the localisation has been directed, not to one Ledger Account, but to one subsidiary book.

From the author's point of view, the chief value of the tabulation of the Ledgers is in the event of it being necessary to convert books previously kept upon single entry into double entry: this is a feat which is sometimes necessary when examining the books of an undertaking about to be converted into a limited company, or when endeavouring to frame a Deficiency Account in cases of insolvency.

AUDIT OF JOINT STOCK COMPANIES.—The chief points arising in the course of the audit of a Joint Stock Company that do not occur in the audit of a private firm may be divided under the following heads:—

- (a) The audit of Share Capital and Debenture Accounts.
- (b) The audit of Dividend and Interest Accounts.
- (c) Compliance with the various statutory requirements.
- (d) Compliance with the Memorandum and Articles of Association, general Statutory Provisions, special Acts of Parliament, or Deed of Settlement.

(a) **THE AUDIT OF SHARE CAPITAL ACCOUNTS.**—The main points are: (1) Does the stated amount of issued capital represent a valid allotment to *bonâ fide* applicants? To ascertain this, the Auditor must see that the amount is within the authorised issue, that the various classes of shares (if there be classes) are in accordance with the memorandum of association and prospectus, that the minutes of allotment are in order, that the allottees have agreed to become shareholders to an extent not less than the amount of their respective allotments,

that the aggregate number of shares actually issued to the various allottees is equal to the total number stated to have been issued, and that the required deposit has been paid. (2) Has the amount stated to have been paid up been actually received in cash, or else in kind under a valid contract duly registered previous to allotment in accordance with the requirements of Section 25 of the Companies Act, 1867, in the case of shares issued prior to the 1st January 1901? Or, in the case of shares issued *after* that date, have a contract in writing, stating the title of the allottee to such allotment, and a return stating the number and nominal amount of shares so allotted, been filed within one month of the allotment, in accordance with the provisions of Section 7 of the Companies Act, 1900? This requires the Auditor to satisfy himself that the minutes making calls are in order, that the amount said to be paid up has actually been received by the bank (application and allotment money and calls should always be paid to the bankers direct), that a valid contract has been registered for all shares issued as paid up, and that shares liable to forfeiture, but not forfeited, appear—so far as can possibly be known—to have been issued to *bonâ fide* existent persons.

PREMIUMS received on the issue of shares should preferably be credited to a special Premiums Account, and it is thought better that they should thus be shown as a separate item upon all succeeding Balance Sheets. There is, however, nothing in the Companies Acts to forbid such premiums being credited to Reserve Fund, or even to Profit and Loss Account.

Since the 1st January 1901 it has been legal for companies making a "public" issue of shares to pay a commission on the underwriting or placing of shares, and provided *any* shares are offered to the public within the terms of the Act, such a commission may be paid not merely in respect of those, but also on all other shares issued by the company. For the payment to be valid, however, it is necessary that the somewhat complicated conditions of Section 8 of the Companies Act, 1900, be strictly complied with.

The above relates to commissions paid out of the capital or shares of the company. Presumably there is nothing illegal in a company applying part of its profits towards the payment of commissions; but, of course, commissions paid for out of profits would necessarily have to be charged against profits, whereas commissions legally paid out of capital might, as a matter of law, be capitalised.

It has been held that the payment of a commission on placing or underwriting shares which is in effect an issue of such shares at a discount, is in all cases illegal; but debentures may be validly issued at a discount.

At subsequent audits it should be ascertained that the Share Ledgers balance; the author never heard it contended that a *full* examination of the Share Ledger was part of an ordinary audit.

So far as the above remarks apply, they will serve to indicate the Auditor's duties with regard to STOCK or DEBENTURES.

(b) THE AUDIT OF PAYMENTS FOR DIVIDEND AND INTEREST is not usually a difficult matter. A list of Shareholders should be handed to the Auditor, showing the number of shares held by each member on the day the dividend was declared, and the amount of dividend due. The additions of this list should be checked, and the totals agreed with the amounts of Shares issued and Dividends payable respectively; it must also be seen that the rate of dividend is correctly calculated *in toto*. In the case of interest on debentures, Income Tax must have been deducted, as also in the case of dividends on shares, unless, indeed, the dividend be on ordinary shares and has been declared "free of Income Tax." A few of the larger amounts, taken at random, may be advantageously compared with the Share Ledger, and the calculations checked; but it is not generally essential that the whole list be exhaustively verified. Many large concerns draw one cheque for the whole amount of the dividend, and pay it into a separate banking account, against which the dividend warrants are issued. Where

this method is adopted, it is a comparatively simple matter to vouch the payments and verify the amount of outstanding dividends—which latter will, of course, agree with the balance of the Pass Book. Where dividends are paid in cash, or by cheque upon the ordinary banking account, the vouching becomes merged in the vouching of the general payments. The outstanding dividends will not be so easily traced, but will present no special difficulty that requires particular mention here.

Interest on debentures, &c., presents no further points for consideration; but it is particularly necessary to bear in mind that Income Tax must always be deducted from interest, and from (maximum) dividends on preference shares, or the ordinary shareholders will suffer an injustice.

(c) THE VARIOUS STATUTORY REQUIREMENTS, above referred to, together with the several sections enforcing their use, are as follow:—

So far as companies registered under the Companies Acts, 1862-1900, are concerned:—

- (a) Register of Members (*vide* Section 25 of the 1862 Act).
- (b) Register of Mortgages (*vide* Section 43 of the 1862 Act, and Section 14 of the 1900 Act).
- (c) Annual List of Members and Summary Book (*vide* Section 26 of the 1862 Act, and Section 19 of the 1900 Act).
- (d) Minute Book (*vide* Section 67 of the 1862 Act).
- (e) Register of Directors and Managers (*vide* Section 5 of the 1862 Act, and Section 20 of the 1900 Act).

The provisions of the Companies Act, 1900, as to prospectus, allotment, statutory meeting, audit, &c., should also be carefully followed.

Companies incorporating the Companies Clauses Act, 1845—that is to say, almost all companies incorporated by special Act of Parliament—are required to keep the following:—

- (a) Register of Shareholders (Section 9).
- (b) Shareholders' Address Book (Section 12).
- (c) Register of Holders of Consolidated Stock (Section 63).
- (d) Register of Mortgages (Section 43).
- (e) Registers of Transfers (Section 15).
- (f) Minute Book (Section 98).

The particulars required to be contained in each of these books may be ascertained upon reference to the sections named, which are reproduced in full in Appendix "A."

In the case of all companies the following statistical books are practically indispensable, whether required by statute or not:—

Shareholders' and Debenture-holders' Address Books.

Share Ledger.

Debenture Ledger.

Transfer Registers (for Shares and Debentures).

Directors' Attendance Book.

Applications and Allotments Book (one for each class of shares or debentures).

Call Books (ditto).

Strictly speaking, there is nothing to audit in these various books—because they are statistical books merely, and not books of account—but the Auditor should satisfy himself that the records are kept in the prescribed form, and, *primâ facie*, correctly. In addition, he will do well to ascertain that all mortgages and charges that require registration have been entered fully in the Register of Mortgages, and a return filed with the Registrar of Joint Stock Companies.

(d) COMPLIANCE WITH THE MEMORANDUM AND ARTICLES OF ASSOCIATION, SPECIAL ACTS OF PARLIAMENT, OR DEED OF SETTLEMENT.—Under this heading it is difficult to profitably draw attention to any specific points. It may be mentioned, however, that it is not

merely expedient, but also absolutely necessary, that the Auditor should carefully peruse such of these documents as may relate to any particular audit, with a view to modifying his course of action accordingly. The special points to which it will be necessary for him to direct attention are, so far as the capital is concerned, as to whether it has been duly authorised and expended upon the objects for which the company was formed; so far as the accounts are concerned, that any special points raised in these documents are borne in mind when considering the method upon which the accounts have been framed; and, so far as the question of profits available for dividend is concerned, as to whether all stipulations as to certain profits being carried to reserve, or applied to the future redemption of debentures, have been properly dealt with.

In the case of companies registered under the Companies Acts it is also desirable that particular attention should be directed to the various contracts connected with the original formation of the company. In all cases the prospectus (if any) should be very carefully scanned, with a view to seeing that any special provisions laid down therein are also included in the regulations of the company, and have been acted upon. It is naturally difficult, if not actually impossible, to speak exhaustively in this connection; but it may be mentioned that, supposing a prospectus states that the directors will not take any fees unless the company has made profits, or until a certain dividend has been paid to shareholders, then, whether or not a similar provision is contained in the company's Articles of Association or special Act of Parliament, it is necessary that the Auditor should see it has been complied with in the accounts which come before him for certification. On this point, however, nothing more than general hints can be given.

The question of Secret Reserves is dealt with in Chapter VI., and need therefore only be mentioned here in passing. As bearing up the question now under review, the decision of Mr. (now Lord) Justice BUCKLEY in *Newton v. The Birmingham Small Arms Co., Lim.*, appears to have been that Articles of

Association which purport to take away from the Auditor his statutory right to report to the shareholders in cases where moneys have been applied in contravention of the terms of the Memorandum of Association are *ipso facto* invalid. This seems to suggest that the duty is imposed upon the Auditor of seeing—so far as he can from careful inspection of the books, accounts, vouchers, &c.—that none of the acts of the directors have been *ultra vires*. In many cases this would appear to throw upon the Auditor a duty so onerous as to be almost impossible of performance; but it emphasises the view laid down in previous editions of this work, that, so far as is reasonably possible, the Auditor should carefully consider this question of *ultra vires*, because an agent acting beyond his authority does not bind his principal, and thus the unauthorised acts of agents may have a material bearing upon the principal's accounts.

CHAPTER II.

METHODS OF ACCOUNT

(Suggested in the Course of Audit.)

IT is not strictly any part of the Auditor's duty to offer suggestions or issue instructions as to the system of accounts to be adopted, but on account of his experience in such matters he is frequently asked to do so. The following remarks will, therefore, not be amiss in the present connection; but it will, of course, be understood that the various questions now about to be considered are, for the most part, largely matters of individual opinion. The views stated in the following paragraphs are but those of the author, and it is by no means suggested that they should be unquestioningly taken on trust by the readers of this book. Circumstances notoriously alter cases, and in no state of existence is this more true than in the realm of accounts.

GENERAL SYSTEM OF INTERNAL CHECK.—This is a matter that may very profitably engage the careful attention of the Auditor, for not only will a proper system of internal check frequently obviate the necessity of a detailed audit, but it further possesses the important advantage of causing any irregularities to be corrected *at once*, instead of continuing until the next visit of the Auditor, which—even in the case of a continuous audit—is clearly a consideration. It is very probable that the Auditor will be asked to make any suggestions that may occur to him for the improvement of the existing system of accounts, or in the case of a new undertaking he may be invited to prepare a system for the use of his clients. In the latter case at least the work is naturally no part of the regular audit, and should command a special fee, but in the former case it would

not usually be regarded as an extra unless the alterations suggested and adopted were of a radical nature.

9. In devising any system of internal check, there are three matters to be specially borne in mind : first, the person in charge of the cash should never be in charge of any Ledger, or, at least, of any Trade Ledger ; secondly, each separate Ledger should be made self-balancing, or at least should be so arranged that it can be separately balanced, and where this is for any reason not altogether practicable, it is absolutely essential that those Ledgers which are not checked in detail should be so arranged that they may be collectively balanced separately from those Ledgers that are ; thirdly, where the Trade Ledgers are numerous and are not checked in detail by the Auditor, the clerks in charge should be frequently changed about, so that if there is any irregularity it is impossible for it to remain long undetected without implicating the whole staff. With a system of accounts arranged upon these lines, a detailed audit is frequently not necessary in its entirety ; but it is always desirable that the Auditor should satisfy himself that the system has actually been carried out as originally designed, and sections of the work should be fully checked at unexpected times.

INSTRUCTIONS AS TO GENERAL SYSTEM OF ACCOUNTS.—It is usually desirable that the head book-keeper should be placed in possession of written instructions containing an outline of the system to be followed. These written instructions will naturally vary very considerably according to circumstances, and it is impossible to give here more than the barest outline of what may be required. The following points are, however, important ones, which will generally require to be included :—

(1) All cash received to be paid into bank daily. The cashier to have no control over any of the Ledgers.

(2) All payments other than petty cash payments to be made by cheque, whatever the amount.

(3) The Petty Cash Book to be kept upon the imprest system under the supervision of the cashier. The clerk in charge of

the petty cash must on no account be allowed to receive any moneys for sundry cash receipts.

(4) Proper Receipt Books to be used for all moneys received, and vouchers obtained for every payment.

(5) The cash and bank balances to be verified weekly, or oftener, and the adjustments recorded in a special Balance Book.

(6) All Ledgers to be rendered self-balancing, and all Trade Ledgers to be balanced monthly. A maximum difference of (say) 1s. to be allowed in any one Trade Ledger, subject to the approval of the head bookkeeper. All such differences to be recorded from time to time in a special book kept by the head bookkeeper.

(7) An adequate system of Stock Accounts and Cost Accounts to be provided.

(8) All invoices for purchases to be passed by the Goods Received Department, by the Buyer of the Department concerned, and by the Counting-House, before being entered in the Purchases Book. ?

(9) Statements for trade payments to be passed by some responsible person, preferably one of the partners, or—in the case of a company—the managing director.

(10) The calculations of all sales invoices to be checked in the Counting-House before the Sold Ledgers are posted.

(11) Each time the Sold Ledgers are balanced a list of all accounts more than —— days overdue to be submitted to the head bookkeeper, and by him to one of the principals for further instructions.

(12) A thoroughly efficient system of calculating and paying wages to be introduced, and closely adhered to.

(13) So far as may be possible the duties of every member of the staff should be varied from time to time.

(14) Every member of the staff should be required to take a holiday at least once a year.

(15) No member of the staff should be allowed to perform what are (for the time being) the duties of another.

In the case of a Company:—

(16) The Minute Books to be fully entered up, and kept indexed to date.

(17) All exceptional transactions to be reported to the Board at the next meeting for approval or further instructions.

(18) The various books required by the Companies Acts to be kept written up, and the necessary returns to be made to the Registrar from time to time.

COST ACCOUNTS.—Every system of Bookkeeping worthy of the name, that purports to record the transactions of a manufacturer, will provide some method of ascertaining the cost of the articles produced, while many systems recording transactions of a purely trading nature (*i.e.*, buying and selling *only*) will likewise find a proper system of costing most advantageous. The fact remains, however, that Cost Accounts, as now arranged, are generally unsystematic, unreliable, and unaudited, and this statement is as literally true to-day as it was when the first edition of this work was published.

It is not proposed to devote any large portion of space to the advocacy of a proper system of costing. Those who doubt its utility will do well to study a paper on the subject by Mr. JOHN MANN, Junr., M.A., C.A. (Glasgow), which appeared in *The Accountant* of 29th August and 5th September 1891, and also a leading article that appeared in the issue of that paper for the 28th November 1891, and many others which have appeared in those columns more recently. The subject is also dealt with in the author's *Advanced Accounting*. If these various contributions have produced no effect, the author doubts his ability to work a conversion, and must, therefore, be content to pass the matter by.

FORM OF CASH BOOK.—A good form of Cash Book not only saves time and trouble every day of the year, but also

—to an even greater extent—when the Ledgers come to be balanced.

It is impossible to go fully into this matter here, but it is suggested that, in all businesses of any magnitude, the Auditor should consider the advisability of recommending the introduction of various columns into the Cash Book that would facilitate the balancing of the various Ledgers employed. In an extreme case, the use of a Ledger might be almost obviated by the use of a numerous-columned Cash Book ; and in many cases a little ingenuity will suffice to materially reduce the labour of posting during the year, and to a corresponding extent facilitate the balancing of the Ledgers at the year's end.

The author has seen a Cash Book ruled with special columns for Bills, thereby doing away with the Ledger Accounts, but in this specific instance the result was not particularly happy. The abolition of the Ledger Accounts (where expedient) is best managed by elaborating the Bill Book into a Bill Ledger.

In large concerns a great saving of time may be effected by assigning a separate Cash Book to each Ledger clerk. These separate Cash Books will, of course, all work into the General Cash Book. (See further, under "Self-balancing Ledgers," *postea*.)

DISCOUNT AND INTEREST.—A considerable amount of time may be saved by a proper system in recording cash discounts. Every trading or manufacturing concern should have Discount columns in its Cash Book ; by which means the necessary number of postings may be considerably reduced. The common practice of posting the total of the debit discount column to the debit of the Ledger, and *vice versa*, is, however, essentially unscientific. An entry should be made at the foot of the debit column for the total amount of discounts received, and posted thence to the credit of the Discount Account ; while on the credit side of the Cash Book an entry is made in the Discount column of the total amount of discounts allowed, which is posted to the debit of the Discount Account. By this means the total

of the debtor and creditor Discount columns will be made to agree—just the same as the two Bank columns, or any other two corresponding columns agree—while the advantage of posting totals to the Ledger Account, instead of differences, is not lost. Moreover, the rule that the debit cash entries are posted to the credit of the Ledger, and *vice versa*, is uniformly maintained, which will always be an advantage theoretically, and—where one is dealing with second-rate bookkeepers—practically as well.

In every case, whatever method be adopted, the total of discounts received should be credited to Profit and Loss Account, and the total of discounts allowed debited. A further consideration arises, however—namely, that, while discounts are theoretically supposed to represent an allowance granted for a payment made before it is due, it is an almost universal custom to deduct discount from all outstanding accounts at balancing time, and to amend the Profit and Loss Account accordingly. The position is not very logical; but where, upon the whole, discounts show a loss, there is much to commend it.

CASH DISCOUNTS (so-called) received on account of Capital Expenditure by a Parliamentary Company are clearly a reduction of such Capital Expenditure.

INTEREST, received and allowed, requires to be separated in the Profit and Loss Account, just the same as Discount; and, where it is desired to reveal the whole effect of the working of a concern, it is advisable to separate Discount from Interest.

The question of outstanding Discount and Interest is dealt with more fully in Chapter VI.

BANK CHARGES.—Before taking leave of the Cash Book, it is well to note that the Auditor might with advantage roughly check the bank charges debited to his client, and see that the rate actually charged is in accordance with arrangements made. Unless thoroughly checked, bank charges have frequently a curious habit of increasing from year to year.

→ PETTY CASH.—The author is acquainted with two good systems of Petty Cash, and with numerous bad ones. It is not

proposed to deal exhaustively with the latter, but a good system is sufficiently uncommon to merit a record in these columns.

The system of debiting Petty Cash payments *en bloc* to Profit and Loss is bad ; and it is therefore assumed that, under each of the following methods, the various payments are periodically analysed. Petty Cash should be balanced at least once a month, and frequently it will be found advantageous to balance at even shorter intervals. The analysis may be made either by means of analysis columns in the book itself, or by a summary written in the book after being prepared on loose dissecting sheets, as may be found most convenient.

Under one system the Petty Cashier is started with an amount, say £20, which is supposed to be more than sufficient for the payments for the month (or whatever other period be adopted). At the end of the month he hands the Cashier a summary of his payments, and receives a cheque for that amount. On the counterfoil of the cheque, the summary (or a reference to it) is written, and the cheque is written up in detail in the Cash Book at once, and thence posted direct to the debit of the various accounts. Under this system no Ledger Account is required for Petty Cash, but an account should in every case be opened for the initial balance, as, if it be left as a floating balance on Office Expenses, or any other Nominal Account, it is apt to get lost sight of. The Chief Cashier should thoroughly examine the Petty Cash Book each time he draws a cheque ; and when the cheque has been cashed, the initial balance should be shown him intact. The Auditor also will, of course, require to see this balance, or to have it properly accounted for.

The other system is more suitable where the expenditure is too large for it to be deemed desirable to trust the Petty Cashier with an amount sufficient to cover a month's expenses.

In this case, there will be a small initial balance, and when it becomes nearly exhausted a cheque will be given for the exact amount spent up to date. This system is thus similar to the

former, but with shorter rests ; but to avoid numerous entries in the Cash Book the cheques drawn (including that for the initial balance) are posted to the debit of a Petty Cash Account in the Ledger. The result of the monthly summary is credited to Petty Cash Account, and debited to the various Nominal Accounts, either by being posted direct from the Summary, or by means of a Journal entry. The balance of the Petty Cash Account at the end of each month will thus always represent the amount of the initial balance.

It will be noticed that debiting Nominal Accounts has always been spoken of. In the comparatively rare cases where it is desirable to make Bought Ledger, and other, payments (which involve the debit of a Personal Account) by Cash, every consideration of convenience will tend to the use of a separate Cash Book for this purpose, which will, of course, be kept upon similar lines to those indicated. Sometimes (as in the case of solicitors) it is better to keep only one Petty Cash Book, but in that case separate columns should be employed for expenses and for payments on account of clients.

Both the above are varieties of the "Imprest System," so called from the demand (or imprest) presented to the Chief by the Petty Cashier from time to time for a sum to reimburse him for his payments.

A good system of Petty Cash is of the greatest value, both to the Auditor and to his clients, and it is therefore always advisable that the Auditor should use his influence in this direction.

RENTS (RECEIVED AND PAID).—Where a considerable portion of the income is derived from the receipt of Rents, it is probable that some reasonable system of Accounts will be found in connection with them ; but where the matter is, so to speak, a side-issue, the probabilities are that there will be found to be no system whatever. Cottages let to workmen are, perhaps, the most ordinary instance of a revenue being incidentally derived from Rents Received ; and, as a rule, the accounts in

connection with them will be found extremely primitive. The usual method is to deduct the amount of rent from each man's pay, and credit the total deductions to a Rent Received Account. This method might answer if the proper deductions were invariably made; but under such a system—if a man were allowed to get into arrear, or if no wages were due to him—the matter is very liable to be lost sight of; and, in any case, no proper record will be kept of any allowances made to tenants for taxes, repairs, &c. In every case, therefore, a proper rent-roll should be kept. In general, this will be found an actual saving of time in the end; and, in any case, it will probably save its cost in the increasing resultant revenue.

Suitable rulings for rent-rolls (for rents payable weekly, monthly, &c.) will be found in the author's *Auctioneers' Accounts*.

The proportion of rent accruing, but not due, should be included in the Balance Sheet as an asset; as also should all arrears, unless, indeed, there is reason to believe that they will not be recovered. All accruing and outstanding liabilities for ground rent, rates, taxes, &c., must also be included, and the Auditor must not be put off with any suggestion that "they about balance one another." What he has to deal with are the facts.

In the case of cottage property, occupied by workmen, it is desirable to show the whole matter in a nutshell in the Profit and Loss Account; therefore show Rents, less Outgoings, on the credit side, and carry out only the net Revenue derived.

Where only a portion of certain premises is occupied, and the remainder sub-let, a similar course should be pursued. That is to say, the total rent paid should be shown on the debit side, the rent receivable deducted, and the net rent paid carried out. It is considered in some quarters that a statement of the net amount is sufficient; but the effect of the sub-let premises becoming vacant should be considered, for if this be neglected, the amount stated in the accounts would be liable to sudden and

unexplained fluctuations. If accounts are intended to show the whole facts of the case, it will be seen at once how defective are statements containing the net amount only.

RENTS PAYABLE.—Where the business is carried on in freehold premises owned by the proprietors, there is no reason why the Rent Account should not be charged with a fair amount for the use of the premises. This practically amounts to the proprietors giving themselves a lease of the property, which naturally leads to a consideration of the question of leaseholds.

WHERE A VALUABLE LEASE is held, for which a premium has been paid, the annual amount written off for depreciation may appropriately be charged to Rent Account, it being, in fact, merely a portion of the rent paid in advance; but it would be well for the accounts to state that this has been done. By “annual payment” it will, of course, be understood that Depreciation, pure and simple, is referred to, irrespective of interest; the Profit and Loss Account must be credited to “Interest on Investments” in the usual way. A useful Depreciation Table will be found in Appendix “D.”

“SELF-BALANCING” LEDGERS.—All Accountants—and, for that matter, most Bookkeepers—will be familiar with the method usually adopted for verifying the accuracy of each Ledger in a system of accounts. It would probably be the exception to find a set of books in which some device for the separate balancing of each Ledger was not in use; on the other hand, the instances in which some properly *organised* system of applying this check has been adopted are probably more exceptional.

The usual method is to take the total of the list of Ledger balances at the previous time of balancing, allow for the total amounts that should have been posted to the debit and credit of the Ledger respectively, and the resultant figure should agree with the total of the present list of balances. This method is often of the greatest possible assistance when dealing with books that have been more or less incompletely kept; but it can

hardly be called scientific, and is, at best, but a convenient makeshift, nor can Ledgers so kept be properly styled "self-balancing."

Every Ledger should be so arranged as to possess within itself all the materials of a Trial Balance. That is to say, each Departmental Ledger should contain a "General Ledger Adjustment Account," while the General Ledger should contain an Adjustment Account for each of the Departmental Ledgers. The detailed consideration of this matter is, however, a question of Bookkeeping rather than Auditing; it will accordingly be found to be fully dealt with in the author's *Bookkeeping for Accountant Students*. The Adjustment Account is a most valuable device, as by this means each Ledger can, at any time, be balanced with the minimum of trouble, and absolutely irrespective of the other Ledgers. Moreover, in the event of any Ledger not agreeing, the side (whether debit or credit) upon which the difference occurs can be readily perceived. Hence it follows that a *rough* Balance Sheet and Profit and Loss Account can always be prepared in a very short space of time, without involving the labour of balancing every Ledger. Again, the clerk keeping the General Ledger (naturally the clerk most to be trusted, if not actually one of the principals, or, perhaps even the Auditors themselves) has a very good check on every other Ledger clerk. *It must, however, never be lost sight of that the only reliable verification of the various balances of the Adjustment Accounts in the General Ledger lies in the thorough verification of the various Departmental Ledger balances.* If this fact be lost sight of, there is a serious risk of fraud; but, if the system be intelligently applied, it is a distinct preventive of any kind of irregularity.

The Auditor who once adopts this system will find it not only lessen his own work and that of the bookkeeper, but also add to the completeness of whatever system may have previously been in use; and, further, materially increase the pleasure attendant upon the investigation. Where the Auditor himself keeps the Private Ledger (a not uncommon practice where private persons

and firms are concerned) the advantage of making each Ledger "self-balancing" must be sufficiently obvious to need no further demonstration.

WHERE A PROPER STOCK ACCOUNT IS KEPT, or there is a reliable means of estimating the amount of Stock on hand (*c.f.* Stock Accounts), the existence of "self-balancing" Ledgers makes it possible for a reliable Balance Sheet and Profit and Loss Account to be prepared, at any time, in a few hours, or even minutes; and the advantage of this—where no Cost Accounts can be kept—is hardly to be over-estimated.

TABULAR LEDGERS.—Another form of self-balancing Ledger—to which indeed the term "self-balancing" may, perhaps, be more appropriately applied than to the kind described in the preceding paragraph—is the Tabular Ledger. This Ledger is suitable to those concerns in which accounts are rendered only at certain definite intervals, and where the number of customers is extremely numerous, while the number of transactions with each customer is but small. These limitations naturally reduce the general utility of Tabular Ledgers, but they are common with gas companies, water companies, electric light companies, and also for the purpose of recording the collection of rates made by various local authorities. In each of these cases the account rendered to the customer virtually consists of a single item, but the same form of Ledger is sometimes found convenient in cases where a large number of items have to be recorded; in these latter cases, however, a subsidiary Ledger has to be kept for the purpose of collecting the items which constitute the account to be collected. Under ordinary circumstances the extra labour involved would go far to prevent the employment of tabulated Ledgers in such cases as this, but it sometimes occurs—*e.g.*, in the case of a colliery—that the daily deliveries are only invoiced as regards weight and quality, without being priced out, and that the subsidiary Ledger is also kept in quantities only; the pricing out being only done when the monthly statement of account is sent in, and this being so, a tabulated form of Ledger might conveniently be adopted in such

a case, although probably the number of accounts would not be sufficient to render such a course imperative.

Yet another form of Tabular Ledger is that in use at hotels. The especial object of this form is to make the Ledger do duty not only as a Personal Ledger showing the state of account between the hotel and the various visitors, but also as a Nominal Ledger showing the analysed receipts from day to day. This form of Ledger is especially applicable to hotels, on account of the large number of nominal accounts employed to analyse the income derived from various sources ; it is also most convenient on account of the fact that it presents the readiest means of keeping each account written up to date, with a minimum of labour.

CARD BOOKKEEPING, &c.—Of late years the “Slip System” of bookkeeping has been steadily becoming more general, and there seems to be every indication that as its advantages become more widely known it will be still further utilised. A full description of the various applications of this system will be found in the author’s *Advanced Accounting*, and would be out of place here. It is necessary, however, for the sake of completeness, to now consider the matter from the point of view of the Auditor. There can be no doubt but that, unless a thoroughly efficient system of account-keeping prevails, the introduction in any form whatever of the Slip System is likely to make confusion worse confounded ; but, given a properly organised counting-house, it seems that practically the only drawback that can be suggested is the increased responsibility that is thrown upon the Auditor of maintaining a vigilant outlook for fraud.

A great deal has been made by some critics of the possibility of Cards, or Sheets, being destroyed, and replaced by others containing falsified entries. With a proper system, however, such irregularities would be more speedily detected than would their equivalent under the old-fashioned system of recording all entries in bound books. Bound books are invariably paged or folioed consecutively, but it is safe to assert that no Auditor ever conceived it to be part of his duty to make sure that the pages or

folios of each Ledger were complete. If a folio be neatly extracted from a Ledger, it is not unlikely that its absence might remain undetected for months, so long as it had not been removed until after all postings to that folio had been checked. This risk has been provided for under all adequate varieties of the Slip System; and it makes but little demand upon the Auditor's time to satisfy himself that there are no cards or sheets missing, and that all those presented to him for audit are the ones originally issued by the bookkeeper.

With both Card and Loose-Leaf Ledgers it is as a rule better to check the postings by calling back from the Ledger into the books of first-entry, as time can generally thus be saved; while this sequence enables the Auditor to more readily satisfy himself that the Ledger, as presented to him for audit, is complete.

STORES ACCOUNTS. — In many businesses it is quite practicable to keep a reliable record of all goods or stores in stock, and—wherever this is possible—it is clearly desirable that the Auditor should place before his clients the indisputable advantages of such a course.

Full details as to the best method to be adopted in all cases would naturally involve a consideration of the particular stocks employed in various trades and manufactures, and would be out of place in this volume, but the following general recommendations (quoted from *The Accountants' Manual*, Vol. II.) will doubtless prove sufficient for the purpose:—

“(1) Debit and Credit Accounts should be opened, as far as possible, for each description of Stores used. On one side of the accounts the receipts would be entered, showing the date, weight, quantity or number, and other particulars; and, on the other side, the stores given out from time to time would be entered, with such particulars as were necessary or suitable, the difference representing what ought to be in hand, or thereabouts—as, in accounts of this kind, the balance shown upon the accounts can hardly be depended upon exactly.

"(2) It is the opinion of practical mill-owners and managers that in many cases a really efficient and exact check on Stores is not practicable. It could, no doubt, be devised; but the detailed work in connection with it, and consequent labour and expense, put it out of the range of every-day business, whatever theorists may say. But many useful rules may be laid down preventive of fraud and waste, amongst others the following taken from actual experience:—

"(a) Where stores are distributed for use upon a specific job, the job should be stated, with the weight, quantity, &c. At Newcastle-upon-Tyne lately, a vast system of fraud was discovered, which had gone on for years; in part through the neglect to adopt the recommendation of the Auditors (Chartered Accountants) that proper Store Accounts should be kept.

"(b) If material of the same kind is distributed to various men for the same purpose, a comparison should be made between the results produced by each. If discrepancies are found, enquiries should be made, and doubtless in some cases a good explanation could be given: *e.g.*, old machinery or appliances, &c.

"(c) The store room should be so situated that people going in and coming out would pass under the eye of the principal, manager, or some other responsible person.

"(d) The principal, or manager, should make a point of examining at times the Stock Ledgers and taking a general supervision of the department. Frequent and unnotified visits should be made, and the storekeeper, *if possible* (it is not always possible), changed [occasionally].

"(e) Some kinds of stores should never be given out unless the used-up stores are returned. For example, a workman making requisitions for files, brushes, and like things, should only be supplied on his giving up the old articles. This is a very good check, when the nature of the stores will allow of its application."

It will be perceived that the above considerations refer primarily to the stores purchased by factories for their own use;

an ordinary amount of intelligence will, however, suffice to render the recommendations there made applicable to a trading concern—that is to say, a concern where the goods purchased are issued (sold) to outside persons. A simple system will be found fully described in the author's *Advanced Accounting*.

In designing Stock Accounts for trading concerns (and sometimes, also, with factories) it is possible to arrange for the keeping of the accounts in sterling as well as in weight or quantity; and, where this can be done, it is clearly desirable—as it is then possible—to make the Stock Accounts part of the regular system of double-entry bookkeeping employed. It is, however, better to retain the record of weights or quantities wherever practicable, as otherwise a discrepancy in quantity might easily be concealed by an error in the values attached to the various stores.

STOCK ACCOUNTS.—With some businesses (especially traders dealing in small articles broken from bulk) a regular system of Stock Accounts is not practicable. In such cases a different method of check must be employed. In every trade there is a well-known percentage of gross profit that ought always to be earned, and can rarely be exceeded. If, therefore, the Stock Account is started with the actual stock on hand at the commencement of a period, debited from time to time (usually monthly) with the total purchases, and also with the aforementioned estimated gross profits on the sales, and credited with the sales, the balance shown will represent the stock on hand—estimated on the assumption that the nominal gross profit has been exactly earned. At the periodical stocktaking this estimate can, of course, be easily verified, or corrected. Where an undertaking trades in various kinds of goods it is always desirable to dissect the sales and purchases, so that the position of the various departments may be readily perceived.

This system is in very general use, and serves two most useful ends. (1) It calls attention to any discrepancy between the actual and nominal gross profits, by means of a similar discrepancy between the ascertained and estimated stock in hand. (2) It affords most useful information as to the probable amount

of stock in each department from month to month, and so serves as a guide to, and a check upon, the various departmental managers, as well as affording material for an interim Balance Sheet, if one be required.

It is, of course, impossible to give any definite information concerning the gross profits usually made in various retail trades. Naturally, everything depends upon the situation of the shop, and the class of business done. The following table of estimated gross profits realised on so-called "Stores prices" by a leading London house will not, however, be without interest:—

Grocery	...	...	10 per cent.
Wines and Spirits	...	...	15 "
Cutlery	...	...	15 "
Drapery	...	...	10 "
Stationery	...	...	15 "
Jewellery	...	...	25 "
Drugs ...	...	...	25 "
Provisions	...	...	8 "
Beer ...	...	...	10 "
Tobacco	...	...	7½ "
Tailoring	...	...	12½ "
Mantles and Dresses	...	...	17½ "
Meat ...	...	...	10 "
Fancy Goods	...	...	17½ "

It is not, of course, suggested that these rates would apply to all houses, selling at "Co-operative prices" (for the very term itself is sufficiently elastic), but they will serve as a useful guide of the gross profit likely to be earned by a house doing a good class of ready-money trade.

It is, perhaps, well to note that, in accordance with the invariable custom of traders, the above percentages are based upon the *selling* price of the goods, and not on the cost price.

It may be added that a comparison of the ratio between the stock-in-trade and the sales during corresponding periods is often useful as a rough test of the accuracy of the stocktaking.

In conclusion, it may be stated that the Auditor who has been requested to design Stock Accounts for any special business will do well to avail himself of whatever practical experience may be possessed by his clients, or their managers. Nevertheless, he should take the earliest opportunity of verifying the experience thus utilised by his own; and, where he should be so fortunate as to possess some slight practical knowledge of the particular business in question—a knowledge he is very likely to have had the opportunity of acquiring in connection with the winding-up of insolvent estates—he will doubtless find it of the greatest assistance.

STOCK AND SHARE ACCOUNTS OF COMPANIES.

—With regard to these accounts, much that might have been said has been anticipated under the heading of “SELF-BALANCING LEDGERS” (*q.v.*). Each class of shares or stock should have an account opened for it in the General Ledger, and such account will, in fact, become the Adjustment Account for that particular Share Ledger. By this means all transfers are kept out of the General Ledger, and—after the issue has once been completed—no further entries are necessary. Should the issue be a large one, however, it is often preferable to open separate General Ledger Accounts for “applications,” “allotments,” and “calls,” respectively.

This system may be greatly assisted by the addition of an extra column to the debit side of the General Cash Book, the items entered in such column being posted to the Share and Stock Ledger, and the totals periodically extended into the Bank column, and these posted to the General Ledger in the usual way. If this method be adopted, the duplication of entries is reduced to a minimum, and the Auditor's work becomes not only proportionately lighter, but also much more certain. With large companies, whose shareholders are very numerous, it is usual to devote a special book to Capital receipts, and carry totals only to the General Cash Book. This system lends itself readily to the method advocated.

For full information upon this subject the reader is referred to the author's *Bookkeeping for Company Secretaries*, or *Advanced Accounting*.

SUSPENSE ACCOUNTS.—Most of the points comprised under this heading will be found to be fully dealt with at a later stage, under the heads of "Outstanding Assets and Liabilities" and "Contingent Liabilities"; but the following, which refer rather to questions of account than to general matters of principle, may be more appropriately considered here.

Any outstanding amounts due, or supposed to be due, either to or by an undertaking, should never be allowed to stand as balances upon a Nominal Account. The great convenience of bringing the balance down on the Nominal Account, as opposed to opening a Suspense Account which will naturally have to be closed the following morning, makes this method of bookkeeping—if, indeed, it can be called a method—a great favourite with a certain class of bookkeeper; but the objections that can be raised against such a procedure are quite sufficient to outweigh any advantages that it may be supposed to possess. From a bookkeeper's point of view, doubtless, the balance on the Nominal Account may be deemed to answer all purposes sufficiently well, but the Auditor must take a higher view of matters. In the first place, the balance is very apt to be lost sight of, and consequently no adjustment made, at the close of the next period—particularly where a standing balance of petty cash in hand is left open upon, say, the Office Expenses Account. Secondly, the method is open to abuse on the part of a fraudulent bookkeeper, and—in the absence of the suggestive headings of Suspense Accounts—the matter might possibly escape the vigilance of the Auditor. And, again, it is a distinct advantage to arrange the Trial Balance so that it may contain, in itself, all the information necessary for closing the books and preparing the Balance Sheet and Trading and Profit and Loss Accounts, and this can only be conveniently effected by making the necessary adjusting entries, by means of Suspense Accounts, before the Trial Balance is extracted.

THE TREATMENT OF BAD AND DOUBTFUL DEBTS.—An intelligent system of dealing with the difficult question of Bad and Doubtful Debts is of such assistance to all commercial houses that the Auditor should lose no opportunity of suggesting that the matter be put upon a scientific basis.

A very good method is the following:—

As soon as a debt becomes at all doubtful, or sufficiently overdue to merit special attention, it is transferred to a Doubtful Debts Ledger, which is ruled as follows: On the left-hand page are spaces for two or three ordinary Ledger Accounts, while the right-hand page is left blank for such memoranda as "When applied for," "When sued," "When failed," and full particulars as to progress of subsequent realisation of the estate. When an account becomes hopelessly bad (either by reason of the Statute of Limitations intervening, or an execution remaining unsatisfied, or a final dividend having been distributed, or a composition accepted), *and not until then*, the Account is written off to Bad Debts Account; but on no account should an amount be written off until it is known to be irretrievably bad, as an amount, once written off, is almost certain never to be recovered. It will be noted that not the least of the advantages afforded by this system is the peculiar prominence it gives to all overdue Accounts, thus offering special facilities for their receiving the particular attention they so urgently require. In a large concern, moreover, it is an obvious advantage that overdue accounts should pass into the control of a different Ledger clerk.

Where it is the custom to pass all overdue debts on to the solicitor for collection, their simultaneous transfer to the Doubtful Debts Ledger provides a convenient record of all matters in the solicitor's hands.

Q The necessary provision for loss upon Bad and Doubtful Debts may be made by means of the Reserve for Bad Debts Account, which may be credited with the estimated amount of such loss, while the Bad Debts (nominal) Account is debited in the usual way. The memoranda recorded on the blank pages of

the Doubtful Debts Ledger will readily afford all available information upon which a proper valuation of the amount necessary to be written off may be prepared, and the systematic focussing of such information upon the method here described will generally admit of a much more reliable estimate being prepared than would otherwise have been practicable.

Some persons prefer to base their valuation upon a certain percentage of the Sales, and so equalise the loss by charging each year only with an average amount. The argument in this case is that the loss was not really made in the year when it was discovered, but in the year when the sale was effected. The contention is ingenious, but not particularly sound. In any case, the Auditor should satisfy himself that the Balance Sheet he is required to certify does not overstate the amount of the Book Debts; on the other hand, there can be no objection to a reasonable reserve being built up to meet losses that may be incurred in the future.

THE USE OF THE JOURNAL.—The extent to which the much-abused Journal may be advantageously employed in modern commercial Bookkeeping is a question upon the discussion of which so much acrimony has already been unprofitably expended that it is with considerable diffidence that the subject is approached at all.

After all has been said, however, the fact remains that many classes of business may, without any considerable loss of labour, employ the Journal for summarising all kinds of General Ledger transactions except cash. In such cases—and, be it noted, such cases are referred to only—it appears to be a considerable advantage to pass the Cash *totals* through the Journal, and so obtain from the Journal the sum total of all transactions, which may be then checked against the *totals* of the Trial Balance, which will be taken out in four columns (upon the French method) for this purpose.

Where this is done, an error in the Trial Balance may be localised, as to debt or credit, and a considerable amount of time will thus be saved in effecting a final agreement.

It is not, perhaps, very often that this method of balancing by totals will be found to be practicable, but it is, at the same time, much more frequently possible than some would appear to think; and the safeguard it affords against fraudulent transfers in the Ledger, between Nominal and Personal Accounts, is an advantage not to be lost sight of where other circumstances are equal.

Where this check of the totals of the transactions is not practicable by means of a regular Journal, it may often be effected by the Auditor constructing an equivalent for the Journal from the totals of various other books, and—where this is practicable—the Auditor should not let the opportunity escape him.

WAGES AND SALARIES.—The best method of paying wages has already been detailed in Chapter I., and therefore nothing further need be said upon that subject here.

SALARIES should, in large concerns, be dealt with in a manner as near thereto as practicable. The distinction made by writers between wages and salaries is by no means invariably clear, and therefore some definition seems desirable. By Wages is meant the cost of labour, and also the cost of the immediate supervision of such labour (foremen, &c.), which would probably be paid for at the same time and in the same manner—in a word, cost of artisans' or labourers' work. By Salaries is meant the weekly or other payments to managers, salesmen, clerks, and other more educated workers. Thus, wages will be always an expense of production; but salaries may be an expense of production, distribution, or administration, although generally one of the two latter. The above definitions are by no means universally accepted, but for present purposes the classification according to method of payment and of audit appears to be the most convenient.

A **SALARIES LEDGER** may be regarded as essential in all but the smallest concerns. An account should be opened for each person in receipt of salary, and the rate and time of payment

stated at the head of the account. Each payment will be entered on the account as made, and duly signed for by the recipient. This Salaries Ledger has, it will be seen, no credit side, and is purely a statistical-book. Many retailers, and others, make a special agreement with their hands so that they may be dismissed without notice; where this is the case the form of agreement may appropriately be printed at the head of each account, and it will be convenient to have a sixpenny agreement stamp embossed upon each page.

The SALARIES BOOK contains a list of each set of payments, the total corresponding to the amount of the cheque drawn, and the items bearing the folios of the various Ledger Accounts.

The Auditor need not do more than check the additions of the Salaries Book and the postings of one or two weeks; but he should take a look through the whole Ledger, page by page, and he should never volunteer to any of the staff the information that he does not check every figure.

AGENTS' ACCOUNTS.—With books which are not kept by very skilled bookkeepers, the Auditor frequently has a considerable amount of additional, and wholly unnecessary, trouble in connection with the accounts between his clients and their agents, or between his clients (the agents) and their principals. It is therefore very desirable that Agency Accounts should be kept upon some definite and practicable system. The conditions of agency are so various that it is impossible to deal in detail here with every conceivable set of circumstances arising in connection with this subject, but it may be pointed out, in general terms, that where the remuneration of the agent is dependent upon the amount of sales or purchases effected by him every consideration of convenience is in favour of a special Sold or Bought Book being employed for his transactions; or, at all events, a special column being devoted to these transactions in the general Sold or Bought Book, as the case may be. When, on the other hand, the remuneration of the agent is by way of profits, or a percentage on the profits earned, whether gross or net, the accounts should be so schemed that an "Agency

Account is opened in the General or Private Ledger, which virtually becomes the Trading, or Profit and Loss, Account in respect of the transactions with which the agent is concerned.

From many points of view there is much in common between Agency Accounts and Consignment Accounts, and therefore the considerations obtaining under the latter heading will frequently be found of use in connection with the accounts between agents and principals, and may be usefully consulted before formulating any definite scheme upon which these latter accounts should be kept.

CONSIGNMENT ACCOUNTS.—It has already been pointed out under the previous heading that the most convenient method of dealing with many Agency Accounts is to so arrange the books that what is virtually a special Trading, or a special Profit and Loss, Account should be kept in respect of these particular items. These remarks apply *a fortiori* to Consignment Accounts. The statement will be found in many text-books on bookkeeping (chiefly, however, of the unpractical order) that when a consignee receives goods for a consignor it is unnecessary that any entry should be made in his books in respect thereof. This, it will be obvious, is a complete departure from the fundamental rule of bookkeeping, which requires that it should be "a record of transactions," and this proposition seems so self-evident that no time will be wasted in more fully discussing it. Apart, however, from this academical objection, it may be pointed out that every consideration of convenience requires that in the books of the consignee there should be two accounts for the purpose of recording his transactions with the consignor; the one virtually a Trading Account, showing the actual result of the trading in the goods consigned, and the other a Personal Account, showing the position between the consignee and the consignor.

Where several consignments are received from the same consignor, a separate Trading Account should be opened for each, but one Personal Account will usually suffice.

The same remarks apply to the books of the consignor himself, except that—as he is dependent entirely upon the consignee for the record of transactions after the goods have once left his office—it becomes possible in some cases to adequately record these transactions in one account. In the vast majority of cases, however, it will be found that two accounts are not only more convenient, but in the long run involve less trouble and time in the keeping.

A fuller and more detailed exposition of the best method of dealing with these accounts will be found in the author's *Bookkeeping for Accountant Students*, to which the reader is referred.

THE ACCOUNTS OF BRANCH ESTABLISHMENTS.—This is a point upon which the Auditor will frequently experience considerable difficulty, by reason of the defective system of record employed, and it is therefore of especial importance in connection with the subject of auditing that a really practical system of bookkeeping should be dealt with in this connection.

It may be stated at the outset that the accounts of Branch establishments may be ranged under two wholly different categories. In the first case, the accounts of the Branch are kept at the Branch itself, and are practically independent of those kept at the Head Office; in the second case, a minimum possible amount of accountancy is employed at the Branch, returns being made to the Head Office, and the transactions of the Branch incorporated in the Head Office Books. The latter class of accounts, of course, present no serious difficulty, and, indeed, for all practical purposes the bookkeeping is the same as though the Branch establishment did not exist, except that for statistical purposes it may be thought desirable that some of the Nominal Accounts should be divided up so as to show the transactions of the Branch separately for purposes of comparison.

It is, however, with regard to the former class that most difficulties are likely to arise. In this connection it may be

pointed out that any difficulty or complication which can be conceived may be at once got over if the system of accounts at the Branch Office be regarded in precisely the same light as though the Ledgers recording these transactions were in point of fact kept at the Head Office in Self-balancing Ledgers, in respect of which Adjustment Accounts were to be found in the Head Office Ledgers themselves. These Adjustment Accounts in the Head Office Ledgers, which, of course, will be written up from returns made by the Branches, will provide the means of controlling the record of transactions in the Branch Ledgers, and at the same time combine the whole system of accounts into one entity. On the other hand, there should, of course, be Adjustment Accounts in the Branch Office Books, so that these themselves may be made self-balancing.

? When balancing time comes it is necessary that a Trial Balance should be taken of the Branch Books, and remitted to the Head Office, and this will be found to explain and verify the Adjustment Account in the Head Office Books dealing with the Branch transactions. The Trial Balance at the Head Office can then be amplified so as to give effect to these records.

Before leaving the question of Branch Accounts it may be pointed out that the balance of expediency lies in favour of the Branch's bank being a branch of the same bank as that employed at the Head Office, so that facilities may be afforded for a prompt return being made to the Head Office of the payments into and out of the Branch's banking account. On the other hand, in many cases it will be found preferable not to employ any banking account of the Branch at all, but to receive and pay all accounts through the Head Office alone; and, where the nature of the business renders this possible, every consideration of expediency will be in favour of its being carried out.

Another point which is well worth bearing in mind, where it can be practically applied, is that with certain classes of business—that is to say, those which deal with the sale of goods in bulk without the bulk being broken, it is of inestimable advantage for the purchases to be all made at the Head Office, and

the goods supplied to the Branch Offices being supplied to them by the Head Office at selling price. The Stock Account at the Branch Office then becomes much simplified, and the balance of such Stock Accounts should represent the stock actually available on hand, without any adjustments being necessary in respect of estimated or actual gross profit. It is not necessary that this system should at all confuse the question of the profits actually earned by the Branch, because there is not the least difficulty in the goods supplied to the Branch being credited to a special account in the Head Office Books, instead of being credited to the general Sales Account.

The mere fact that a business has numerous branches, instead of merely one, in no way alters the fundamental principles on which the accounts of these branches should be kept; but it need hardly be added that it enormously increases the arguments in favour of these Branch Accounts being organised and rigidly kept upon a thoroughly sound basis of internal check, and one which renders itself readily available to the scrutiny and supervision of the Auditor.

Full details of the manner in which Branch Accounts should be kept will be found in the author's *Advanced Accounting*.

CAPITAL AND REVENUE.—The distinction between Capital Expenditure and Revenue Expenditure is one of primary importance, as bearing upon the fundamental question of what profits have actually been made by an undertaking during any given period. But it is thought that much unnecessary complication has been introduced in discussing this subject, and that, when these wholly irrelevant matters are brushed aside, the fundamental question will be found to be simplicity itself.

Shortly stated, the question can in any event be answered by finding the answer to the following question: "Has the particular expenditure incurred in any individual case been incurred for the sake of improving the earning capacity of the undertaking?" If the answer to this question is in the affirmative, then, and to that extent, the expenditure in question is Capital

Expenditure. But if it has only had the effect of putting the earning capacity of the undertaking upon the same footing as that which had previously obtained (and which has since declined by the ordinary process of wear and tear, or the effluxion of time, in respect of which no provision has been made) it must be charged against Revenue. The precise meaning of this latter qualification is that the mere *renewal* of wasting assets, not otherwise provided for, cannot be called capital expenditure, but that any extension, or the acquiring of fresh assets, is in the nature of capital expenditure.

It may be added that it is generally supposed that Local Authorities are allowed to issue loans to cover Capital Expenditure, but that all Revenue Expenditure must be met out of current Revenue—*i.e.*, spontaneous income, trading profits, or rates. In general terms this is doubtless so, but “short loans” are not infrequently sanctioned for renewal purposes where some slight improvement is effected simultaneously—*e.g.*, repaving streets with a more suitable material. On the other hand, when considering Capital Expenditure that may be met by the issue of loans, it is the usual practice of the Local Government Board to disallow for this purpose all such expenditure as represents Wages paid to workmen in the permanent employ of the Authority, even although such payments are solely in respect of work which accountants would regard as pure Capital Expenditure. Business undertakings would see no difficulty in capitalising all expenditure which tended to improve, or enlarge, the general equipment of the business. For instance, an engineering company (unless it wished to create a Secret Reserve) would invariably treat as assets the machines or tools manufactured in its own factory for its own use; and similarly practically all Capital Expenditure incurred by (say) a railway company would (in so far as it consisted of Wages) be paid to permanent employees. The rule of the Local Government Board already referred to is doubtless convenient, and affords a safeguard against abuse that can be readily applied; but it cannot be regarded as affecting in any way the principles underlying the proper distinction between Capital and Revenue Expenditure.

INSTRUCTIONS AS TO PREPARATION FOR AUDIT.—As a fitting conclusion to the present Chapter, a brief list of instructions—such as might be prepared by the Auditor for the guidance of the bookkeeper, showing the work that should be done before the audit commences—is appended. Such a list is the following:—

(1) All postings should be completed, all additions inked in, all balances extracted, and the Trial Balance agreed.

(2) Vouchers for all payments should be arranged in order, and available.

(3) A complete list of all books, with the names of the clerks in charge of each, should be prepared.

(4) If possible, the cash in hand at the date of closing the books should be paid into the bank; but, where this has not been done, the cashier must have his books written up to date, and the vouchers ready.

(5) A complete inventory of the stock—priced, extended, added, and duly certified—should be ready.

(6) All bonds, bills, deeds, and other securities should be ready for production when called for by the Auditor, and a list thereof should be prepared.

(7) A list of all overdue accounts showing the provision (if any) which it is deemed necessary to make against possible loss should be prepared.

(8) A memorandum should be kept of any other matter to which it is thought desirable to call the Auditor's attention.

(9) A draft Balance Sheet and Profit and Loss Account should be prepared.

As has already been pointed out, some of the duties comprised in the foregoing may devolve upon the Auditor in the case of a private firm or trader; but in the case of a company audit it is particularly desirable that these matters should be

completed before the Auditor commences his investigation, as it cannot be too strongly impressed upon all concerned that the accounts submitted to the shareholders are *not* the Auditor's accounts, but the accounts of the directors.

CHAPTER III.

SPECIAL CONSIDERATIONS IN DIFFERENT CLASSES OF AUDITS.

IN the previous chapters the rules laid down have been of as general a character as possible ; but it must not, therefore, be supposed that the audit of every concern is to be carried out on precisely the same lines. The opportunities for fraud will vary widely in concerns of a different character, while the chances of unintentional errors of principle and in detail will likewise vary extensively in different classes of concerns.

As has been already intimated, the Auditor who wishes to be of the greatest possible service to his client should avail himself of every opportunity to become practically acquainted with the working of the business, as it will only be when he has some real acquaintance with the matter he is discussing that his opinion upon the accounts of any given business will possess any great weight ; for if he has no knowledge of the business carried on it is impossible for him to intelligently criticise the system of accounts that records the transactions effected, and if he has no knowledge of the nature of such transactions it is hardly to be expected that he should be in a position to form any reliable opinion as to the risk that exists of the transactions not being correctly recorded in the accounts. These remarks will, perhaps, appear trite to many, but so much has been said about Accountants "confining themselves to their own province" that it has become necessary to point out the utter inefficiency of any audit which confines its investigations to an inquiry as to the academical correctness of the bookkeeping.

The object of the following chapters is not to supply the reader with such special knowledge concerning each class of undertaking as it may be desirable for him to possess before presuming to certify as to the correctness of its accounts—such a knowledge cannot be altogether imparted by any book, and is beyond the scope (as it is beyond the compass) of the present volume—but in the following paragraphs the reader will find his attention directed to those points most worthy of his consideration in each of the leading classes of accounts he is likely to be called upon to verify. The special opportunities of fraud, and the points upon which an innocent misstatement of facts is most likely to occur, will, so far as possible, claim attention; while it may be added that *The Accountants' Library* provides a series of handbooks dealing with the accounts of most of the leading industries, and is likely to prove useful to the reader—whether practitioner or student.

With these preliminary remarks, the categorical consideration of the subject will be proceeded with.

I. COMMERCIAL ACCOUNTS.—(a) MERCHANTS AND WAREHOUSEMEN.—The chief openings for fraud in these accounts are: Theft of stock; misstatement of cash sales; fraudulent payment of bogus purchases; misappropriation of moneys received in payment of accounts—such accounts being either left open or written off as “bad”; petty theft by the raising of fictitious items of discount allowed on receipts, or interest incurred on payments; and similar matters. Of what may be styled “innocent” errors, the most common are errors of principle in the valuation of stock-in-trade; insufficient depreciation on leases and furniture; omission to allow for outstanding discounts and interest; errors of principle in the valuation of foreign currencies; omission of liability on outstanding expenses, and on bills discounted; insufficient provision for bad debts, &c. There are not many trade details that the Auditor will require to be acquainted with in these accounts, but he will do well to ascertain the terms of payment and discount accorded

to, and by, his clients, and to make use of this knowledge continuously. Where the terms vary—and they generally *do* vary—they should be written in red ink at the head of each account in the Ledger. The Auditor should make himself acquainted with the percentage of profit expected by his clients, and should compare it, both with the actual results and the rate generally realised by others in the same trade. Stock Accounts *can*, almost invariably, be kept by merchants and warehousemen; but this is, in practice, only occasionally done—*verb. sat.*

The question of Patents or Trade-marks sometimes arises in these accounts, but the consideration thereof is more appropriately dealt with in a later chapter.

(b) MANUFACTURING TRADERS.—Under this heading are intended to be included those manufacturers who ordinarily keep a stock of ready-made articles, and who do not manufacture exclusively (or principally) “to order.” Such manufacturers are, clearly, also warehousemen, and consequently the preceding paragraph (a) will apply to the consideration of their accounts; but a few additional precautions are required in connection with their manufacturing departments.

The item of Wages, in particular, is one requiring the utmost care; and the question of Depreciation of Plant and Machinery will also require a full share of attention. A proper system of “costing” becomes all but essential. It is probable that the Auditor will find some such system in operation; but it is at least equally probable that the actual system employed will be found both unscientific and unreliable.

(c) RETAILERS.—RETAILERS WHO GIVE CREDIT in many respects follow upon the same lines as the wholesale houses in the same trade; but the increased number of transactions renders a detailed audit more difficult. It is generally quite impossible to call back all the postings of the Sold Ledger; but the *balancing* thereof can be checked without difficulty, and must always be done. Where practicable the posting of the cash

received may be checked with advantage, and the list of balances should always be compared with the Ledger, and the additions checked. Where the business is very voluminous, the audit of the Sold Ledgers is frequently deputed to some of the counting-house staff; but, in any case, the Auditor should not lose his grip of this department, and should occasionally check the balances himself. To check, say, one or two Ledgers at random each year will have all the moral effect of checking the whole set.

Many retail houses supply goods to their own assistants, &c., at reduced rates, and allow credit until the following pay-day. A separate "Assistants' Ledger" should always be kept in these cases, and the Auditor is usually expected to see that the payment of these accounts is not unduly delayed. At every stock-taking he should be careful to ascertain that no amount stands to the debit of an employee who has left.

The Bought Ledger is generally of comparatively manageable proportions; consequently it is rarely impossible to check it *in toto*. In any case the Bought Ledger payments should be checked, both as to postings and vouchers. In a continuous audit it is frequently arranged that the Auditor shall pass all the Bought Ledger statements for payment, and the system has much to recommend it. In addition to seeing that each item on the statements is also in the Ledger, the Auditor should make the Ledger-keeper initial—and so guarantee the correctness of—every statement that is submitted by him. The Auditor should also compare the discount deducted with the terms of payment stated at the head of each account in the Ledger. It need hardly be added that this passing of the Bought Ledger statements for payment is not a necessary part of any audit, and—where performed—it should command a special fee.

The vouching of cash received—whether for cash sales or Sold Ledger Accounts—may, under a good system of internal check, safely be left to the care of the staff; but it is the Auditor's duty to see that the receipts are duly banked, and to verify the bank balance. A large retailer's audit will, almost

invariably, be continuous; and it is desirable that the bank balance, and also that of the Petty Cash, be examined at least once a month.

The examination of Petty Cash has already occupied attention (*vide* Chapter I.), and it therefore only remains to add that—in addition to vouching for the *bona fides* of all payments—it is essential that some responsible person be made accountable for the correctness of the dissection of the items.

The Departmental Accounts must not be lost sight of, as they form one of the most important branches of the Auditor's duties. An account showing the sales, purchases, and estimated stock should be submitted to the principals each month, and the preparation of this account frequently devolves upon the Auditor. At the stocktaking the reconciliation of the estimated figures with the actual stock on hand may also profitably occupy the Auditor's attention.

The postings of the Private Ledger should always be called back, and it is highly desirable that such Private Ledger should contain, within itself, all the materials for a Trial Balance.

Bills Receivable will but rarely be found in connection with a retailer's business; but Bills Payable are almost certain to exist, and will require attention.

The vouching of payments for salaries must not escape attention, but it calls for no special comment here.

In CASH BUSINESSES the problem is somewhat simplified by the considerable reduction effected in the number of Sold Ledger Accounts. Indeed, these accounts are, of course, naturally abolished *in name*; but they remain, in essence, as Deposit Accounts kept by regular customers who wish to avoid the trouble of remitting with every order. It is an important part of the Auditor's duty to see that Deposit Accounts are never overdrawn without proper authority.

The system adopted for checking the accuracy of the Cash takings will, as before, require the Auditor's careful consideration; but, in the absence of any special arrangement to the contrary, it is not necessary for him to carry his investigation into the accuracy of such takings beyond seeing that the system in use is properly carried out, and that the stated returns are duly banked.

It is very useful for credit notes to be issued against goods returned by customers; and, as these credit notes may be used in payment of subsequent purchases by the customers, or the money therefor obtained upon application to one of the cashiers, the question has to be dealt with by the Auditor. It is generally arranged that, at the end of the day, the petty cashier shall redeem all credit notes in the hands of the receiving cashiers, the amounts being charged up through petty cash. The issue of credit notes must, therefore, be carefully guarded against abuse; and it is essential that the system under which the various departments are debited with their respective returns be properly arranged. The credit notes should always be compared with the counterfoils, and presented to the Auditor for cancellation.

Many retail "limiteds" adopt a similar method for the payment of all dividends under, say, two pounds. In such cases the Auditor's duties are naturally similar to those in connection with credit notes.

(d) CONTRACTORS.—Under this heading the accounts of those manufacturers who keep little or no ready-made stock will be dealt with. This class includes builders, engineers, shipbuilders, &c.

In these accounts the cost of—and profit or loss arising from—each contract will require to be separately stated; the contractor, in fact, opening a special Trading Account for every contract. Cost Accounts thus form an especial feature of the contractor's books, and an inquiry into the principles upon which

they are based is thus a most profitable occupation for the Auditor.

The systems upon which Stores are issued, and Wages booked and paid, are also of the greatest importance; and time spent upon such an inquiry is likely to be of considerably greater advantage to the client than any detailed examination of the books.

The extent of the Auditor's examination into detail will be a matter depending largely upon the nature and magnitude of the undertaking. A detailed audit would not usually be necessary, as the main points could generally be accomplished by an examination of the General Ledger; in any case the *leading principles* will be the really important matter.

The same rules which have already guided the Auditor as to the extent of his inquiry into details will serve him here; the larger the undertaking the more its opportunities of internal check, and consequently the less necessity for the skilled Auditor to check every detail. Many large undertakings keep their own staff Auditor, who is responsible for the technical accuracy of the Trial Balance.

The valuation of Contracts in hand and the calculation of Depreciation are both matters of the greatest importance, but they will be more conveniently dealt with at a later stage (*see under those headings in Chapter VI.*).

(e) BREWERIES.—Although the audit of a brewery is a matter concerning which some experience upon the part of the Auditor is especially desirable, it is by no means easy to indicate, in a few words, the salient features of the task before him.

Theft of stock and of collections are, perhaps, the two main risks run by brewers. The former is best guarded against by properly designed Stock Accounts, and the comparative statistics deducible therefrom, combined with a certain amount of practical knowledge—which latter the Auditor will most likely have to take upon trust from the master brewer. The second risk arises

from the fact that accounts are frequently collected by the draymen ; the matter therefore requires great care, but it presents no exceptional features. The discounts allowed must not be passed without inspection, however, as they can easily be juggled with.

?

In connection with Tied Houses, the Auditor should see that all the revenue receivable from this—as well as from every other—class of investment is brought into the account, subject only to due provision for bad and doubtful debts. In most cases Loans will be due from the tenants of these houses, and in connection with these Loans provision against loss is a matter of considerable importance, and one requiring the most careful consideration. It should moreover be borne in mind that the limit of possible loss in most cases greatly exceeds the amount actually advanced, inasmuch as the Brewery will usually have guaranteed a Loan obtained by the tenant, which forms a first charge upon the property. The aggregate amount of such guarantees should, it is thought, be in all cases stated upon the Balance Sheet as a contingent liability.

Another point of considerable importance is the question of Depreciation. In the case of a Brewery plant the actual wear and tear is probably less than in the case of most undertakings, because the plant will not be working every day, and thus—apart from the fact that it is running a comparatively small number of hours per week—the intervals of rest afford facilities for making satisfactory and permanent repairs to a far greater extent than is practicable with most other undertakings. The result is that a Brewery plant can in practice be kept at a very high state of efficiency by careful and reasonable repairs and renewals. On the other hand, some items are especially liable to depreciation by becoming obsolete, and this important fact should not be lost sight of.

The reader who is desirous of obtaining more detailed information upon this class of accounts is referred to “Brewers’ Accounts,” by Mr. WILLIAM HARRIS, A.C.A.

(f) HOTELS.—The accounts of hotels, whether belonging to companies or to private persons, do not call for any extended comment. The Auditor who is accustomed to Hotel Accounts will be able, by a careful examination of the items comprised in the Profit and Loss Account, to form a fairly reliable opinion as to whether or not any leakage exists. If there appears to be any reason to suspect that things are not as they should be, it might be found desirable to thoroughly examine in detail the charges for a portion, at least, of the period under consideration; but, under ordinary circumstances, it is not usual to carry the investigation *behind* the Bar Bill Book (or Visitors' Ledger) except for the purpose of verifying the Cellar Stock Books. Proper Stock Accounts ought always to be kept of wines, spirits, &c., and these should be carefully inspected, especially if the Profit and Loss Account does not show an adequate return on this department. Where the bookkeeper is also the cashier, especial care must be exercised to ascertain that all receipts are properly accounted for; and it is also important to see that the petty cash disbursed upon behalf of visitors has been duly charged to their accounts and collected. The entries in the Tradesmen's, Nominal, and Private Ledgers should always be thoroughly checked; and especial care should be given to the vouching of all payments, including wages.

/ The question of Depreciation—here, as elsewhere—is also a most important one, and must be carefully considered. Such items as Bedding and Linen, Plate, Cutlery, China and Glass, &c., are frequently re-valued for each Balance Sheet, instead of being depreciated regularly; but perhaps a better plan is to debit Profit and Loss Account and credit Renewals Account with a fixed (ample) provision for renewals, the actual expenditure being debited to Renewals Account, and any credit balance treated as a Reserve. The advantage of this course is that it equalises profits, so that a period of five years could be averaged; but it is well for the Auditor to satisfy himself that the amount written off against Revenue is ample for all ordinary contingencies.

PUBLIC HOUSES follow, in many respects, the same lines as Hotels. The accounts are, in some ways, simpler; but, on the other hand, they are generally less complete. An experienced Auditor may prove himself of considerable value to the proprietor of a public house, but he cannot pretend to protect him against fraud on the part of his employees; neither is it always possible for him to detect any fraud that may have been committed. He can, however, prepare—or superintend the preparation of—accounts that will show exactly *how* the net profit has been earned, and these accounts will suffice the experienced client, for he knows exactly what result ought to have ensued from a given turnover, and so can judge for himself as to the satisfactoriness of the existing management.

With regard to the effect of the Licensing Act, 1904 (*vide* Appendix "A") on the accounts of undertakings owning licensed properties, it is thought that all annual payments to the Compensation Fund should be treated as Revenue charges: if a licence is withdrawn and compensation received in respect thereof, the transaction should be treated as though the licence lost had been *sold* for the sum received, thus resulting in a loss chargeable against Revenue or a divisible profit, as the case may be. If licences belonging to neighbouring competitors are withdrawn, an indirect benefit may quite possibly result; but such benefit (if any) does not appear to be sufficiently definite or direct to justify the capitalisation of any portion of the annual payments made to the Compensation Fund under the Act.

(g) CLUB ACCOUNTS.—The accounts of clubs follow very much upon the lines previously indicated with regard to hotels; but there are one or two points with which it seems desirable to deal in a little further detail. In the business of an hotel it is, of course, practically impossible for the proprietors to rely upon their customers to in any way assist them in checking their employees, but, in the case of clubs—and particularly members' clubs, where the members themselves are the proprietors of the undertaking—the accounts can be, to a certain extent, modified with advantage with a view to devising a system by which the

members themselves may, to a certain extent, check fraud upon the part of employees.

In many clubs the system obtains of requesting members, after they have paid their bills at the cashier's desk in the coffee room, to place the receipted account in a locked box standing near. The receipted accounts thus form vouchers which can be utilised as the best possible check upon the cashier himself. In the billiard room, too, it is a very usual custom for members to be asked to place their table-money in a locked box, instead of giving it to the waiter, as is invariably done at hotels; and by this means one of the chief difficulties which arise in connection with hotels is obviated, it being well known that in most hotels the proprietors do not get the benefit of the full earnings of the billiard tables. Other points of a similar description will frequently suggest themselves to the Auditor from time to time. To a great extent they will assist him in making his audit more thorough, and will sometimes enable him to dispense with details of checking which otherwise would be absolutely necessary.

In connection with the cellar, also, the accounts of clubs present an advantage over those employed by many hotels, viz., that all orders for drinks have (frequently) to be signed by the member and are thus available as vouchers for verifying the taking of wines and spirits out of stock. It may be added, however, that this is a system which is used by a considerable number of hotels, although many dispense with it on the ground that it is difficult to get their customers to take the necessary trouble.

(h) THEATRE ACCOUNTS, &c.—The most difficult feature in theatrical and similar accounts (from the Auditor's point of view) is the large amount of cash—*i.e.*, coin—which is necessarily handled by all persons connected with the financial part of the management. With the exception of the sums received from the "Libraries," almost all the receipts will be in hard cash; and, on the other hand, it is not infrequent to find that the whole of the amount paid out weekly in salaries and

wages is likewise in the coin of the realm. Experience seems to have taught all persons concerned the peculiar charm attaching to a "metallic" currency; and although, from their point of view, there is doubtless much to be said in favour of the system that so generally obtains, the liability to loss—arising from either carelessness or fraud—is sufficient to make many wish that theatrical credit was sufficiently free to permit of a more extended paper currency—in cheques, at least.

An Auditor must, however, above all things be practical: and it is, therefore, well to face the situation at once, and do his best with the existing cash system, for he may rest assured that no amount of "representation" upon his part will induce managers to make all their payments by cheque, while it is, of course, quite impossible that their receipts should be, to any great extent, in anything but cash.

It is not usual for the Auditor to be expected to verify the cash takings: this office is usually performed by the Treasurer, or (in a touring company) by the business manager, who is considered a sufficiently responsible person for the performance of a function that requires integrity certainly, but no great technical knowledge. It should be an invariable rule that all sums received are banked at least once a day, and the Auditor will probably find no great difficulty in securing the adoption of this plan. Where this is done he will, of course, satisfy himself that the amounts so banked agree with the various returns that have been certified by the Treasurer. As these returns have not been prepared by the Treasurer himself, they form a fairly reliable check upon that official, and—under a properly arranged system of internal check—are sufficient for all practical purposes.

- Payments may be roughly divided into three classes—(1)
? Mounting Expenses, (2) Advertising, (3) Running Expenses, viz.,
(a) salaries and wages, (b) rent, gas, &c. &c. The first will almost entirely be paid by cheque, against accounts properly certified by the manager, and call for no special comment. The same remark applies to advertising, which, by the way, is almost

invariably done by a contractor. Salaries and wages are always paid in cash, usually weekly: separate pay-sheets are drawn up for (1) "Front of house," &c., (2) principals, (3) chorus and ballet, (3a) "supers," (4) band, (5) wardrobe, (6) carpenters, &c. It is a good plan to have separate cheques drawn for each of these headings, and to let every employee sign for the amount paid him. "Supers" do not usually sign for their wages, however, the super-master's signature being accepted for the whole amount paid. (In exceptional cases, however, the salary of some great "star" will be paid into his or her banking account direct: such transactions are, of course, easily vouched.)

The vouching of payments thus resolves itself upon the lines ordinarily adopted in trading concerns; and here—as elsewhere—it is not the least important of the Auditor's functions to inquire into the manner in which the pay-sheets are prepared. It need hardly be stated that all persons entering the premises before a performance sign an Attendance Book kept at the stage door for that purpose, and that fines for absence or lateness are arrived at from this source. It is not usual for the Auditor to verify the composition of the pay-sheets, but there would be no harm done if he did so occasionally—and unexpectedly.

Advances, or "subs.," are frequently made to members of touring companies (and occasionally also in town companies), and it generally happens that the result is chaos. The Auditor will do well to inquire into the system in vogue as regards "subs.," and to see that it is such that the paymaster (and not the proprietor) loses by any careless omission to recover a "sub." out of the following week's salary.

The valuation of assets, especially of copyrights and performing rights, is, perhaps, almost the most ticklish matter in connection with theatre audits; but the subject is so technical that it is necessary to dismiss it with a passing caution against over-valuation. It will be best for the Auditor to expressly state in his report that he does not accept any responsibility for the values placed upon these assets.

When a company is "on tour"* the usual arrangement is to divide the gross receipts in fixed proportions (generally half each) between the "company" and the provincial lessee, the latter paying rent, gas, &c., also "front of house" and carpenters' wages (sometimes, also the band), and advertising. The duties of an Auditor acting for either side are thus somewhat reduced. When acting for the representatives, or proprietors, of the touring company he will base his item "gross receipts" upon the joint-certified return of his client's business manager and the provincial treasurer (who is, not infrequently, stage manager and lessee as well). He must, of course, see that the proper percentage of these gross receipts is duly accounted for. Railway charges will usually be arranged with the companies from head-quarters; and hotel accommodation is not generally provided in theatrical companies.

In the case of CONCERT PARTIES on tour it is, however, still sometimes the practice for the management to pay hotel bills. These should be produced to the Auditor as vouchers; but, of course, many incidental expenses must be accepted on the sole statement of the business manager.

Refreshments and advertising on programmes are usually sublet; if not, see under HOTELS (I. f) and PUBLISHERS (I. j) in this chapter.

(j) PUBLISHERS.—The audit of Publishers' Accounts presents a peculiar combination of complications. In many cases publishers will do their own printing, and in this respect they follow the rules of manufacturing traders (see under heading I. (b) above). Almost invariably, however, they will also be retailers, and hence the considerations detailed under heading I. (c) will also apply. Many houses add the further occupation of trading, either wholesale or retail, or both, in the publications of other firms, which, to a great extent, brings them under the heading I. (a) above; while almost every house will

* For this purpose suburban theatres rank as "provincial" theatres, and the companies appearing there are said to be "on tour."

occasionally undertake the publication of authors' work upon such terms, as to royalty, &c., as make it absolutely necessary that both Stock Accounts and Cost Accounts should be carried to perfection. In this respect Publishers' Accounts involve many of the considerations discussed under heading I. (d) when dealing with Contractors' Accounts.

A complete audit of Publishers' Accounts is, on account of the multiplicity of detail involved, a practical impossibility; the extent to which a partial audit may advantageously be carried must, on the other hand, of necessity vary with almost every individual case. The considerations involved in the previous paragraphs are the only ones that can be offered; but it may be added that here—as in the case of all other partial audits—the precise routine may be *varied* from time to time with the greatest advantage.

Advertisements inserted in books, and also in magazines, are a source of income that must not escape attention. It frequently happens that the whole space has been sold out-and-out to an advertising contractor, which will naturally simplify the Auditor's work to a great extent; where, however, a firm of publishers runs its own advertising department—an unusual occurrence with books, but not an infrequent practice with magazines and reviews—the procedure follows that of the Newspaper audit, which will be considered next. As to how far the Auditor need go into detail here, must again be left greatly to his own discretion and the circumstances of the individual case.

Permanent assets, such as buildings, plant, &c., must, of course, be subjected to proper depreciation, and Stock-in-Trade will require carefully valuing. It ought to be possible for the Auditor to obtain absolute proof as to the *quantity* of Stock-in-Trade, but he can hardly be expected to check the inventory *in extenso*. The prices set upon unsold publications should never exceed the cost of production, and—in the case of periodicals at least—only a certain number are really worth more than waste-paper price.

Care should be taken to ascertain that the Stock List is not unduly inflated by almost entire editions of absolutely unsaleable publications that are not worth anything like the cost of production.

With regard to the valuation of copyrights for Balance Sheet purposes, it is usual for a separate account to be opened for each publication, which is, in the first place, debited with the actual cost of production, including, of course, the printing, binding, illustrations, &c. (and, where the copyright is purchased, the purchase-price thereof, together with that of any stock which may have been taken over therewith). Many firms at balancing time review the debits to the various Copyright Accounts, depreciating some and appreciating others; that is to say, the system is adopted of valuing the copyrights by inventory at each period of balancing, wholly irrespective of the actual cost. It is, of course, very desirable that where necessary the cost should be written *down* from time to time; but the arguments with regard to the writing up the value of a copyright are precisely those which might be—and, indeed, should be—invariably used *against* writing up the value of the asset Goodwill and crediting the difference to Profit and Loss Account. It may be perfectly true that a large revenue is expected from this asset in the future; but that, in itself, can afford no possible argument for anticipating that revenue, and taking credit for it in the current period. On the other hand, it will probably be generally admitted that no great harm can be done by writing up such copyrights as have appreciated, so long as the actual effect of so doing is not to increase the book-value of copyrights as a whole. In this connection it may be mentioned that with many houses there is a good general rule in use, to the effect that the value attached to any copyright should not exceed three years' purchase upon the gross profit earned therefrom during the past year.

Sometimes, even when a publication is itself a failure, some residual value will attach to illustrations, &c., which have been used in its production. It is very important, however, that no

fictitious estimate should be put upon the value of such doubtful assets as these, and of the two it seems infinitely preferable that they should be stated at *nil* in the Balance Sheet.

The value of artists' original drawings (for illustrations) is often considerable, and has not infrequently been found to exceed the price originally paid for both original and copyright. It is hardly safe, however, to reckon such originals as assets—if valuable, they will generally be sold, and, if retained, the most that can be said is that they have a latent value.

On behalf of his clients it may be thought desirable for the Auditor to thoroughly check all Royalty Accounts, but this does not form part of a regular audit.

NEWSPAPERS and PERIODICALS present a few special features. In the absence of a staff-Auditor, the Auditor will require to satisfy himself that every advertisement is eventually paid for (unless, of course, a bad debt has been made), or else that it has been franked as "free" by some responsible person. The Commission Accounts of agents and canvassers should also always be examined.

The "inside" of a paper is the work of the regular staff, or of "contributors"; the former are paid a regular salary (usually), the latter are paid for the actual work done. It would be a desirable thing to make sure that a contributor was never paid for a sub-editor's work, but no Auditor could ever ascertain such a thing for himself, and he must therefore rest content with the certified Contributors' Accounts as they are submitted to him.

It frequently devolves upon the Auditor to prepare weekly, or monthly, Statements, showing approximately the income and expenditure. Such work naturally commands a special fee.

The printing of the publication calls for no special comment here; when done by the proprietors they will, of course, be printers as well as publishers, and the Auditor must take his stand accordingly.

The number of copies printed, issued, returned, exchanged, distributed free, and in stock, should always be certified by the

publishing manager. From his returns the Trade Ledger debits may be vouched.

Every periodical is started at a loss, and it is usual to debit this loss to an Establishment Account; when the concern pays—and so acquires a goodwill—the cost of such goodwill is represented by the amount to the debit of Establishment Account, which thus virtually becomes a Goodwill Account. There is no great objection to this system, and it is much in favour on account of the information it affords to the intending purchaser of a recently established paper; but, when a periodical is once fairly started, the Auditor should require a very good reason to be furnished him before he sanctions the transfer of an unexpected loss to the Establishment Account: if such loss arises from an increase of matter (in quantity or quality) or a reduction in price, it may be in the nature of capital outlay, as tending to increase the permanent value of the concern, but an *unexpected* loss is likely to have the contrary effect.

II. MINING ACCOUNTS.—(a) **COLLIERIES.**—Better advice can hardly be given to the Accountant who is about to audit the accounts of a colliery for the first time than to suggest that he should make a tour of the whole works (both above and below ground) in company with the colliery manager. If he be of an observant turn of mind he will probably, by the end of his inspection, have formed at least some idea of the scope of the undertaking, and he will doubtless find that the gloom of the underworld has thrown considerable light upon the records kept above ground. Even the Auditor experienced in Colliery Accounts will probably find that the thorough inspection of a new mine is really a wise economy of time; in fact, whatever the nature of the business may be, the Auditor who acquaints himself with the manner in which it is carried on does wisely.

A question of particular importance in these accounts is the treatment of the Capital Expenditure Account. Great care must be taken to see that no expenditure properly chargeable against Revenue is included herein—indeed, it is always desirable to

get the Capital Expenditure Account altogether closed as quickly as possible.

1 The item "Minimums paid in excess of Royalties earned," which frequently occurs as an asset in the accounts of young collieries, requires some little explanation. The royalty payable is based upon the quantity of ore extracted—usually upon the number of tons, but sometimes upon the number of cubic yards, or the acreage of the seams worked—a fixed "minimum" or "dead" rent being payable in any event, whether the mines are worked or not. During the sinking of the shafts and first working of the mine, therefore, the rent paid naturally exceeds the normal percentage upon the output. Under ordinary circumstances this would represent a charge against Revenue in the usual way; but, as the lessees are empowered to recoup themselves out of subsequent raisings, it is quite justifiable that the excess so paid away at first should be carried forward as a set-off against the output of later years. It is very necessary, however, that the Auditor should examine the constitution of the amount so carried forward. It not infrequently happens that the mine as a whole is comprised of several leases, some of which are not being worked, and never will be; the minimum rent upon such portions ought, of course, to be charged against Revenue each year, and where, in the early days of the colliery's existence, an accumulation of such minimums has been allowed to be carried forward, it must be written off as soon as possible. Again, there is often a limit to the time during which over-paid royalties may be recouped, and this limit, of course, must not be exceeded. It need hardly be added that the only justification for treating the whole—or any portion—of the balance of the Redeemable Dead Rents Account as an asset is the reasonable probability that it *will* be redeemed out of future workings within the time limit allowed by the lease.

1 The question of Depreciation upon Mines is naturally one of no slight importance; but it would appear that—however desirable it may be that an adequate provision should be made for depreciation arising either from the exhaustion of minerals,

or from the lapse of the lease, or from both—it is not legally necessary even for a mining *company* to set aside any portion of its earnings to replace wasting capital. The Auditor can thus do no more than advise the extreme desirability of so prudent a course.

¹ Depreciation of Plant should, of course, be provided for; but that question is best dealt with in a later chapter, where, also, the proper mode of treating Wagons on the Hire-purchase System is considered in Chapter VI.

BRICK WORKS.—It is a matter of constant occurrence for a colliery to own brickfields, and it is by no means uncommon to find that it owns the cottages occupied by its workpeople. Both these matters will require the Auditor's attention, but they need not be considered at length here. Chapter II. has already dealt with the question of Rents Receivable, while the accounts connected with brickmaking call for no special comment, beyond the mention that proper Cost Accounts must, of course, be kept.

The WAGES paid at collieries require the same careful attention that must at all times be accorded to this most important item; but inasmuch as the great bulk of wages paid is at the rate of so much *per ton*, the aggregate amount payable can be tested with greater facility than in many cases.

The peculiar conditions obtaining to Colliery Accounts generally render it desirable that the audit should descend into somewhat considerable detail; concerning the actual extent of such detail, however, no general rules can be given, as each case must be judged upon its own merits. Great care should be taken to see that no expenses are capitalised that are not *bonâ fide* of a "capital" nature.

(b) FOREIGN MINES.—To a very great extent the foregoing considerations apply to mines of every description; but the circumstances of a mine being abroad naturally modifies the procedure in certain respects. Among other things it should be ascertained that all mining regulations of the foreign (or

Colonial) Government have been complied with, and all taxes and licences paid.

It is not usual for the Auditor to visit the works of a foreign mine. The general manager remits periodically a certified return of his receipts and payments, which is incorporated in the accounts kept at the Head Office. Such accounts are not usually very voluminous, and are generally examined by the Auditor *in toto*. It is, of course, desirable that all expenditure at the works be properly vouched, and for the Auditor to examine these vouchers. To make such an examination really effective, some knowledge of the language locally spoken is, of course, highly desirable; but it is no use for Auditors to conceal (from themselves) the fact that, with regard to foreign expenditure, they are largely in the hands of the Mine Manager, who—up to a certain extent—might rob his employers with impunity, if he so chose.

For Balance Sheet purposes the Mine Manager should be required to apportion all expenditure between Capital and Revenue, and to certify such apportionment; also to submit a certified statement of local floating assets and liabilities, or a certificate that no such assets or liabilities exist locally, and at the same time he should report upon the state of efficiency of the plant and machinery, together with any buildings and other more or less permanent assets there may be upon the works. This latter report is most essential for a proper consideration of the question of depreciation.

It is always well—and where the produce of the mine is precious, it is very essential—for the Auditor to use every available means of ascertaining that credit has been taken in the books for the value of the whole of the output. In conclusion, it may be added that he should expressly state in his report what the precise extent of his examination has been.

(c) MINES UNDER THE STANNARIES ACTS.—It is not usual for the services of professional Auditors to be requisitioned in these cases; but as the Cost Book System under which

the Cornish mines are worked is one peculiarly suitable for Mining Accounts, and as, moreover, the system is not generally known in this country, it has been thought well to state briefly the outlines of its working. Auditors will find it may (so far as legally possible) be advantageously applied to the working of any metalliferous syndicate.

The owners of a mine are practically unlimited partners, with power to transfer their shares without the consent of their co-partners, or to withdraw altogether upon payment of their share of the current liabilities. No partner is liable for the mine's debts, after he has sold or relinquished his share in the mine.

The capital is unlimited. At the commencement it is usual to call up what is considered to be sufficient working capital for the next three months, and thereafter a general meeting must be called at least once in every sixteen weeks. At every meeting an account of receipts and payments and a detailed Balance Sheet must be submitted. If there be a surplus, the members are to decide whether the whole or any (and, if so, what) portion thereof shall be divided. If there be a deficit, a call should be made, sufficient to meet all outstanding liabilities and to provide further working capital for current needs.

There are two methods of paying the miners. "Tributers" are placed on a definite pitch, and are paid a certain agreed proportion of the value of the metal raised by them. Contracts with Tributers are renewed every eight weeks, and their earnings naturally vary very considerably. As they have to pay for candles, dynamite, fuses, tools, &c., they may even find themselves indebted to the mine at the end of their eight weeks' contract; on the other hand, their earnings are sometimes very high. The other method of payment is by "Stoping," under which the miner is paid so much per ton for all stuff (earth and ore) sent to the surface: under this arrangement a miner's earnings are much more regular.

In Appendix "A" will be found certain extracts from the Stannaries Acts relative to accounts under the Cost Book System. It may be added that a very similar system of working mines is very prevalent in Australia, where it is known as the "No Liability" System.

III. FINANCIAL ACCOUNTS.—(a) **BANKS.**—In dealing with the question of Bank Audits it is well to remember that one of the most controversial subjects relative to professional practice is being discussed. So far as possible, a position that few will care to assail will be occupied; but it were well to admit at once that the author considers the duties of a Bank Auditor to be very much more onerous than some eminent Accountants care to admit, whatever his bare legal responsibilities may be. It is not necessary to criticise the motives that have dictated the position taken up by some of the leading members of the profession; but it is difficult to see the force of an argument that virtually amounts to the assertion that the mere multiplicity of a series of statements is a valid reason for not inquiring into the accuracy of those statements. Further, it is to be remembered that the bare legal responsibility is not the highest measure of the duties of a professional man. It is certainly very desirable that the law should not be unduly harsh—or the position of an Auditor would be intolerable—but it is imagined that few would consider that they had discharged all moral obligations as soon as they had complied with their statutory duties. These remarks, however, apply equally to all classes of audits.

Under the Companies Act, 1862, (Section 44)—for which see Appendix "A" to this volume—limited banking companies are required to exhibit a statement of their affairs. It were well, therefore, for the Auditor to see that this section is complied with, and that the statement so exhibited is correct.

In the Companies Act, 1879 (the relevant sections of which are also reproduced in Appendix "A"), various provisions occur with regard to the Auditor's duties which must not escape the

attention of the Auditor of a banking company registered under that Act. The Court of Appeal has decided (in the *London and General Bank* case) that an Auditor appointed under the 1879 Act is an "officer of the company" within the meaning of the Companies (Winding-up) Act, 1890.

One of the provisions of the 1879 Act is that the Auditor (shall be furnished with a list of all books kept by the company, and it is not at all a bad plan to ask for this in other cases besides banks. At the trial of a defaulting bank manager some years since, it transpired that such a list had never been furnished to the Auditor, and that the books that would have revealed the frauds were likewise kept back. The matter provoked some correspondence at the time, but the moral is so obvious that it need not be enlarged upon here.

The certification of a Bank Balance Sheet involves the thorough examination and exhaustive testing of every account in the General Ledger, the counting of the balance of cash in hand, the examination of all bills (especial care being taken to note that all overdue bills are properly explained, and that rebate of interest is duly allowed for at a uniform rate), and the inspection of all securities—in which latter task it is usual for the Auditor to receive the advice and assistance of the Solicitor. With regard to the counting of the cash balance, the only safe way of dealing with cheques in hand is for the Auditor to himself forward them to the Clearing House and other agents. The disregard of this precaution has left the door open for most serious frauds upon the part of bank managers and others.

In connection with the inspection of securities, it is, perhaps, well to call attention to the extreme importance of *all* the securities being produced simultaneously, and of their all remaining in the Auditor's sole keeping until the inspection of all is completed. Extensive frauds have been known to remain undetected through failure to observe this simple precaution.

How far the Auditor should extend his examination of the customers' accounts is a matter concerning which considerable

difference of opinion obtains; but many will endorse the *dictum* of the late Mr. SLOCOMBE, that "the overdrawn balances due from customers should be carefully scrutinised—more particularly those which are not secured, or, being secured, have exceeded the limit fixed by the Board of Directors; and I need not add here that one important part of the Auditor's duty, after making this examination, is to see that, in his judgment, ample provision has been made for the losses likely to arise upon them."

This point suggests the consideration of Secret Reserves, which have been attacked upon the contention that, by their very existence, they proclaim the fact that the Balance Sheet is not "full and fair." Assuming, however, that the Secret Reserve is merely a *bonâ fide* provision against unforeseen bad debts, the author fails to appreciate the crying need for the publication of the amount of the provision made. Unless the amount is so separately stated, however, the *only* proper method of dealing with it is to deduct the amount of the reserve from the assets against loss upon which it has been accumulated. Any such reserve as is implied by the omission of such tangible assets as office premises from the Balance Sheet can only be regarded—and this is stated deliberately, and in spite of the prevalence of the custom—as incorrect and misleading. Moreover, it possesses the practical disadvantage that the very existence of such assets may be concealed even from the Auditor, and thus fail to be examined along with the rest of the securities.

But while frankly admitting that the abuse of Secret Reserves is to be deprecated, the author has been unable to find any justification for the view, which appears to have been entertained by a majority of the Council of the Institute of Chartered Accountants, that the existence of such Secret Reserves must of necessity so vitiate the accuracy of a Balance Sheet as to make it a "false statement" within the meaning of the False Statements (Companies) Bill, 1904. In a sense it is, no doubt, perfectly correct to state that *no* Balance Sheet has, in point of fact, ever yet been prepared which subsequent events showed

to have been absolutely accurate ; but, on the other hand, a Balance Sheet is not—and does not purport to be—a statement of facts, but rather an estimate of a position of affairs which, by its very nature, *cannot* be accurately determined. A reasonable discretion must therefore in all cases be allowed to those responsible for the preparation of a Balance Sheet ; and so long as that distinction was exercised in good faith, and reasonably, no question of “ false statements,” within the meaning of the Bill referred to, could possibly arise.

Perhaps the chief difficulty in the audit of a large bank consists of the great number of its branches : of the English banks alone, eight have over 100 branches. It is expressly provided in the 1879 Act that the Auditor need not examine the accounts of any branch beyond the limits of Europe : this provision certainly relieves the Auditor, so far as it goes, but it is distinctly suggestive of an intention, on the part of the Legislature, that the accounts of all European branches *should* be examined by the Auditor. The difficulty in the way of such an examination in the case of the largest banks must be at once apparent, for obviously it is of but little use for the Auditor to check the cash balances at the various branches unless the checking is conducted simultaneously. It is believed that only one large bank (the Metropolitan) submits all its branches to the Accountants' audit ; still, the existence of a single instance seems to show that the requirements of the statute are not altogether impracticable. It is clearly desirable, where an examination of all the branches has not been made, that the Auditor's certificate should be so framed that there may be no misapprehension upon this point.

A detailed audit extending to all the transactions of a bank is not practicable, nor—in view of the very highly developed system of internal check employed—is it necessary. The branch managers and branch inspectors must perforce be relied upon to a very great extent, and—except in the very rare instances of conspiracy between them—it is thought that they may be safely depended upon. Here, as elsewhere, however, a

knowledge of men and matters is most valuable, and the Auditor should not dismiss this question of possible dishonesty from his mind until he has reasonably satisfied himself upon the point. These remarks are in direct contradiction to the view expressed by Lord (then Mr.) Justice VAUGHAN WILLIAMS in the *New Oriental Bank* case, but it is believed they will be considered practical by many whose authority upon such matters is perhaps even greater.

It is not usual for the Auditor to examine all the customers' Pass Books, but he should see that they are frequently examined by the manager or the inspector, and that every Pass Book has been examined and initialled by one or other of these officers at the close of each half-year. It will be noted that later on (in the case of Building Societies and Trustee Savings Banks) it is laid down as an essential that all Pass Books should be examined by the Auditor: the distinction between the two cases lies in the vastly superior system of internal check adopted by banks.

A plan that is sometimes adopted, and which has much to recommend it, is for the bank to send a statement to every customer, showing the amount to his credit (or debit) at the time of balancing, and requesting him to sign and return the same, if correct. The system is, however, not very usual, and, apparently, when tried has not always been found effective, owing, doubtless, to the unfortunate (but none the less well-known) disinclination of the general public to co-operate with any business undertaking in any reasonable system of check upon the honesty of employees.

It will be observed that the view adopted here with regard to a Bank audit is that the verification of details may, and indeed must, to a large extent be left to the staff audit. The recent frauds upon the Bank of Liverpool, which paid upwards of £170,000 upon cheques forged by one of its Ledger clerks, may perhaps raise a question as to whether this reliance upon the system of internal check is altogether justified in practice.

It is thought, however, that the Liverpool frauds have little, if any, bearing upon the point, in that the system of internal check seems to have been chiefly conspicuous by its absence, or at least by its inefficiency. Three of the fundamental rules of any effective system are: (a) That no clerk should have access to books recording entries which go to check the entries kept by that clerk. (b) That the clerks should be shifted about at frequent intervals, so that a fraud—even if committed—may be speedily detected by a fresh clerk going over the same ground. (c) That no unusual entries, as, for example, transfers, should ever be made without special authority. None of these rudimentary precautions appear to have been adopted in the case mentioned, and it seems safe to say that, had any one of them been in force, the frauds could not have been committed, or would at least have been discovered at a very early date. At the same time, as has already been stated elsewhere, it is always desirable that an Auditor, when considering the exact extent of his investigation, should make careful inquiry into the system of internal check employed, and satisfy himself that the system theoretically in force is actually carried out in practice.

In dealing with Bank Accounts, and all other accounts of a similar nature, the Auditor must never forget that his responsibilities are not confined to safeguarding the interests of the proprietors. His certificate is virtually—whatever it may be legally—a guarantee *to the public* that the accounts submitted are to be relied upon as being, in every respect, correct. It is not, of course, suggested that he guarantees the safety of the customers' deposits; but he would reasonably be blamed were it to transpire that a bank which he had certified as solvent was afterwards discovered to be hopelessly insolvent.

At first sight it may appear impossible for the Auditor to act up to the position here indicated, but he must remember that, in reality, *the* test of an Auditor's competency is in his ability to judge of the correctness of items by an exhaustive testing—not necessarily of the items themselves, but of their totals. Mr.

J. SUGDEN STOCKS, whose experience of Banking Accounts is considerable, has given it as his opinion that "an Auditor, in a comparatively short time, may go through the books of a bank, and satisfy himself as to its thorough stability, without having—as someone has said—to take his seat in the bank parlour and continue his investigations through the whole year." It need hardly be added, however, that a knowledge of banking theory and practice will be found an all but essential aid for this purpose.

The foregoing quotation would seem to imply that Mr. STOCKS considers an annual audit sufficient; but the author considers that a bank audit—to be really effectual—should be more or less continuous, for it is extremely difficult for the Auditor who is not frequently on the spot to get any extensive insight into the manner in which a business is carried on.

A few remarks concerning the Revenue Account will not be out of place. The items of interest constituting the gross profit must be carefully tested, especially as to the rate charged upon current transactions, and also interest taken credit for upon doubtful advances, will require the most careful consideration. With regard to the rebate upon bills in hand, it has already been stated that this should be at a uniform rate; by this, however, is not meant that the rate must necessarily be a fixed one. Some banks employ a fixed rate (generally 5 per cent.), while some employ the rate actually charged in each case; and some, again, the current market rate. The first and third methods possess the merit of simplicity, but perhaps the second is the most strictly accurate. The great thing for the Auditor to observe, however, is that one method is uniformly adopted, otherwise the profits of the year might easily be manipulated.

In the foregoing remarks the desirable extent of the Auditor's duties has been stated rather than the bare limits of his legal responsibilities; the question will, however, be found more fully discussed under the heading of "The Liabilities of Auditors."

(b) INSURANCE OFFICES.—It will be convenient to deal first with Fire Offices, and to afterwards consider the various

modifications necessary for the audit of other Insurance Accounts.

FIRE OFFICES.—The first point appears to be for the Auditor to satisfy himself as to the total amount of income receivable. The Policy Book and the Renewal Register—modified by the “Specials” and Endorsement Books—will provide him with this information: but a large amount of tedious (although most necessary) checking of additions must be done before the result is finally arrived at. Where renewal receipts are written out for *all* existing policies, the production of all unused receipts should be required as a voucher for policies discontinued; but where blank receipts are used—either in the head office, or at the branches or agencies—the number of receipts issued, used, and returned, must be compared with the number of renewals and discontinuances, allowance being made for such receipts as have been spoiled.

It is not necessary for the premium income to be checked in detail; the gross amount receivable is known, and the insurances discontinued can be verified, the net amount receivable can thus be arrived at. The total cash received on account of premiums, less the outstanding balances at the commencement of the period, will agree with the net amount receivable, less the balances outstanding at the close of the books. A list of these latter will be furnished to the Auditor, which he can easily check by satisfying himself that they have either been actually received since the closing of the books, or have been acknowledged by the agents to have been received by them. This is a much smaller affair than checking each item received, but it is—if anything—more exhaustive.

Re-insurances will, of course, require due examination, but they call for no special comment.

The Cash Book must be carefully added and properly vouched, and it is well to check the vouching of all miscellaneous receipts in detail. It is not usually a very long job, and cannot well be verified in any other way.

With regard to losses, it is not usual—unless the amount is large—to go behind the voucher for the receipt of the amount paid; the directors who signed the cheque are supposed to have satisfied themselves (and to have undertaken the responsibility) concerning the *bona fides* of the claims allowed. The postings of the Cash Book should, however, all be checked. It is well to call for the Claims Book, with a view to making sure that due provision has been made among the liabilities for all claims received in respect of losses incurred up to the date of balancing.

The valuation of the Balance Sheet assets is more appropriately considered in a later chapter, while the method of verifying the items is similar to that obtaining under Banks and kindred associations.

The percentage of premium income to be carried forward as a provision against unexpired risks must not be lost sight of. From 30 to 33 per cent. is the usual allowance; if a smaller amount be reserved, the effect is that the company is not setting aside a sum that would be sufficient to enable it to re-insure against the whole of its liabilities under current policies. It should be added that the premiums due at Christmas are *not* included in the accounts drawn up at the close of the year. It is not usual to make any *special* reserve for this purpose: in general, the provision is included in the Reserve Fund. Such a practice is not strictly correct, however, for a Reserve Fund should represent an accumulation of pure profits, while a reserve for unexpired risks is a provision for profits as yet unearned. Still the practice is so general that it can hardly be described as misleading.

Another similar item that must not be forgotten is that of premiums paid in advance. Where a reduced premium is accepted for, say, seven years' premium paid in advance, the question of interest ought really to be considered; but as these transactions are not generally very numerous, interest is not usually provided for.

The item "Premium Income" should always be stated "less Re-insurances," both for the sake of showing the net revenue of the company and for calculating the provision for unexpired risks.

The accumulated reserves of a sound company should always amount to at least one year's net premium income—in some of the best offices they run as high as two years' income.

LIFE OFFICES are governed—so far as the form of their accounts is concerned, and in many other respects of less immediate interest to the Auditor—by the Life Assurance Companies Act, 1870, and the amending Acts of 1871 and 1872. The material portions of these Acts are included in Appendix "A," and should, of course, be thoroughly mastered by the Auditor before commencing his work.

Where the office also carries on other insurance business, it will be noticed that the life accounts are required to be kept separate, and the Auditor will naturally have to see that this is done—not merely on paper, but in very fact.

Every three, five, or seven years (as may be required by the constitution of the company) a "valuation" Balance Sheet will have to be prepared. The distinguishing feature of these periodical accounts is, of course, the actuarial valuation of the office's liability to the policy-holders. The Auditor is not responsible for the accuracy of this valuation, but it is his duty to see that the accounts are duly prepared in accordance with the actuary's figures.

For the benefit of the reader who has had no acquaintance with Life Insurance Accounts, it may be stated that the annual Balance Sheet and Accounts are purely *interim* accounts, and that it is only when the periodical "valuation" takes place that a real balance is struck, and the profit ascertained. The method of arriving at the profit upon these occasions is in reality by single-entry. That is to say, the present value of the existing assets is put down upon the one hand, and upon the other the

present value of the liability on current policies (the total of the actuarial valuation), to which are added the ordinary outside liabilities and the paid-up capital. The difference between these two sets of figures is the profit for the period, subject to any interim dividends that may have been paid or interim bonuses that may have been declared. A careful perusal of the statutory form of accounts appearing in Appendix "A" will enable the reader to clearly follow the procedure indicated.

It has been stated that this assertion, that life insurance companies ascertain their profits by single-entry, is inaccurate, and it has been suggested that the term "single account" should be substituted. Before arriving at any definite conclusion upon the point it is necessary that all parties to the discussion should attach the same meaning to the terms employed. Strictly speaking, there is, of course, no such thing in existence as single-entry, for even under the imperfect systems of account that are ordinarily so described a very considerable proportion of the transactions are invariably recorded by double-entry. The term "single-entry" is ordinarily employed—and has been invariably used by the author to describe *all* systems of bookkeeping that *fall short of complete double-entry*. A complete system of double-entry not merely involves the mechanical record of each transaction once upon each side of the Ledger, but the framing of that record so that at the close of each financial period the nominal accounts may be summarised in a Revenue Account (by whatever precise name, or names, that account may be styled), thus enabling the actual profit—or loss—to be ascertained from the books, and the *means* by which it has been caused to be also clearly shown. A system of accounts which does not enable a proper Revenue Account to be compiled is of necessity incomplete, and is therefore described as a single-entry system.

It may, of course, be argued that in the case of every trading, or manufacturing, concern it is impossible to construct a "pure" Revenue Account, in that the item "Sales" is not a "pure" Revenue item, and has to be counter-balanced by a *contra* item "Cost Price of Goods Sold" (or its equivalent, Purchases *plus*

Wages, as adjusted by Stock at the beginning and end of the period). In a sense that is no doubt true, and in so far as it is true the accounts of all trading or manufacturing concerns are less perfect than those of other undertakings; but there is a vast difference between the method of arriving at the profits of a trading or manufacturing concern (which involves the preparation of an inventory of unsold Stock, but in other respects consists in the focussing together of pure Revenue items) and the method of arriving at the profits of a life insurance company, which is for all practical purposes identical with the method of arriving at the profits of an undertaking whose books have been kept by single-entry. A perusal of the "Valuation" Balance Sheet of any life assurance company will clearly show this.

The routine of the audit will differ but little from that of the Fire Office, but the Auditor will be wise to pay particular attention to the surrenders. Claims should also be more carefully looked to than is necessary in Fire Offices.

The audit of the investments will be a much more voluminous matter than before, and will require considerable care, both to see that the capital is intact and that the prescribed income has been received. As, however, the method of keeping Investment Ledgers varies very considerably with different offices, this matter cannot well be gone into in further detail

In some cases the Auditor of a Life Office will have been appointed especially to protect the interests of policy-holders. In every case, however, the Auditor should consider himself responsible to the policy-holders for the correctness of the accounts, which he should on no account unqualifiedly certify, unless he is convinced of the stability of the undertaking.

ACCIDENT, GUARANTEE, AND OTHER OFFICES do not raise any new considerations. The great majority of such accounts follow entirely upon the lines of Fire Offices—the company's contract being an annual one, which they can discontinue at any time, should they think well to do so. The business of SICKNESS

ASSURANCE, however, more nearly approaches that of a Life Office, and actuarial assistance will be required for the determination of the value of the unexpired risks. No special legislation has been enacted relative to Sickness Assurance Offices.

GENERALLY, readers may be referred to the remarks concerning "Branches" under the head of "Banks." The amount of audit bestowed upon the various branches of Insurance Offices is often by no means sufficient; but, on the other hand, the internal audit is usually fairly satisfactory, while that in force at the head office is, as often as not, most conspicuous by its absence.

It is but right to add that many insurance offices are incorporated either by special Act of Parliament, by Deed of Settlement, or by Royal Charter. This circumstance, however, while naturally affecting the internal arrangements, does not practically influence the Auditor's duties in any material way.

(c) TRUST AND INVESTMENT COMPANIES.—The accounts of these companies are, probably, as simple as accounts can well be. The ostensible purpose of such companies is to enable investors to spread their capital over a large field, and so, by the principle of average, obtain a better security for their principal without a corresponding sacrifice of interest.

How far the Trust Companies of the day have acted up to this theory of their existence it is beyond the present purpose to inquire. Suffice it that, from the shareholder's point of view, the only satisfactory accounts will be those which indicate a fair rate of interest earned without depreciation of capital.

The Auditor will require to see Brokers' Contract Notes for all sales and purchases, and also to ascertain that all dividends and interest have been properly accounted for. Purchases *cum* ? *div.* and sales *ex div.* will probably be the most likely cases in which an irregularity may occur. Only income earned during

the time that an investment is held should be credited to Revenue, while *per contra* Revenue is entitled to take credit for *all* the income earned during that period.

The valuation of investments is perhaps the most important function of the audit of Trust Companies. Under the existing unsatisfactory state of the law, the Auditor cannot, of course, prevent the directors issuing accounts stating investments at cost price (regardless of value), but he at least can—and certainly should—call attention in his report to anything that he considers to be an undue inflation of assets.

It is not always imperative that investments should be written down to market price. In the first place, the principle of averages may consistently be followed here, and it will suffice if the total market price be not less than the total cost price. If, however, there be a deficiency in this respect, it should be met, not by a revision of individual values, but by a setting aside of a lump sum to an Investment Fluctuation Account as a reserve against loss. This reserve may either be deducted from the amount of investments in the Balance Sheet, or separately stated as a liability. A reserve so created should, except in very special cases, not be reduced in subsequent years, except for the purpose of providing for the actual loss realised upon the sale of depreciated investments.

When the total market value exceeds the total cost price it is not at all desirable that the capital value of the investments be increased. To credit such an increase to Revenue is clearly as incorrect as it would be to credit it with an assumed increase in the value of Goodwill. There is no particular harm in writing up the assets and crediting the difference to a Reserve *not* available for equalising dividends, but it is much better kept in hand—at all events until the permanence of the increase be well assured—as a secret reserve, against which the company may draw in bad times.

With regard to the profits or losses arising from sales made during the period under audit, in the first place the dividend

should be apportioned (from day to day) so that the actual capital profit or loss may be arrived at. Such profits and losses made during any one year should be treated in the aggregate: if the result be a profit it is available for dividend; if a loss be the result, it should come out of revenue, unless an adequate reserve exists from which the loss may be taken. It is, however, highly desirable that profits made by changes of investments be taken to reserve, and not credited to revenue.

In bad times the conscientious Auditor of Trust Companies has an unthankful task before him, but he must not shrink from the responsibilities of his situation.

What has been written above appeared in the first edition of this work, when Trust Companies were still in their infancy. It does not seem, however, that more recent events in any way affect the general principles laid down with regard to the manner in which a Trust Company may be soundly conducted. The past years have, in point of fact, proved exceptionally trying to many of the Trust Companies that were in existence when the first edition of this work appeared, and it may be added that the causes of the downfall of the majority of those companies that failed, or were reconstructed during that period, are to be found in their disregard for the principles of sound finance which have been already enumerated.

It has throughout been the general scheme of this work to lay down the lines upon which an audit may be best conducted, rather than those upon which it may be conducted without personal risk to the Auditor himself; but for the sake of completeness it is desirable to call attention to the fact that it has been decided by the Court of Appeal in the case of *Verner v. Commercial and General Trust* that a pure Trust Company may by its articles of association provide that all sums received as interest or dividends upon investments (less administration expenses) are profits available for dividend, without taking into consideration any depreciation or loss arising from fluctuation in the value of the capital assets of the company. The

judgment of the Court of Appeal will be found duly recorded in Appendix "B"; it may, however, be added at this point that the view taken by the Courts seems to be that it is quite competent for a company to so constitute itself that its members are, for all practical purposes, in the same position as life-tenants would be in the case of an ordinary trust; that is to say, they are to receive whatever income is earned (less current expenses), without any reduction in respect of losses of capital or any accretion in respect of gains. Of course, in the case of an ordinary trust the field of investment is expressly limited to first-class securities unless the instrument creating the trust enlarges the field. In the case of a Trust Company the instrument creating the Trust is the memorandum of association, and if sufficiently wide powers are contained in the memorandum it seems to be possible for the company to invest in the most speculative concerns without making any provision for possible or ascertained losses so long as creditors are not defrauded thereby. The decision is in itself sufficiently dangerous, even when expressly limited to a pure Trust Company; but when the decision comes to be further extended, the expediency of following it becomes even more doubtful. In Appendix "B" will be found a report of Mr. (now Lord) Justice STIRLING's judgment in the case of *Wilmer v. McNamara & Co., Lim.*, which is founded upon the decision just stated, but further extends it, for the Court declined to interfere in the distribution of a dividend declared in the case of a trading company, notwithstanding the fact that it was not satisfied that a sufficient sum had been set aside to meet the depreciation that had actually occurred in the wasting assets. Should such a decision as this be upheld upon appeal, it would almost appear as though due provision for depreciation was an entirely voluntary act which could in no case be enforced upon a company against the will of the majority; but the truth of the position seems to be that in this case—and, for that matter, many other similar cases—the attitude taken up by the Courts has been that they cannot undertake to act as "a providence" to all and sundry. So long as creditors are not

defrauded, and so long as persons are not induced to take shares by misrepresentation, the Courts leave each separate company to work out its own salvation upon its own lines.

It is important to distinguish between Trust, or Investment, Companies, and speculative Finance Companies. The chief profits of the former are income derived from investments, and profits derived from a change of investments only arise incidentally. In connection with the latter the profits derived from a change of investments form the main source of income; consequently all such investments must be regarded as so much Stock-in-trade—as floating assets—and valued accordingly, whereas the investments of a *bonâ fide* Trust Company may fairly be treated as fixed assets. The importance of this distinction lies in the fact that whereas the investments of a speculative Finance Company ought *never* to be valued at a price in excess of the current market price, it is frequently difficult (if not impossible) to arrive at any reliable basis of valuation; for Stock Exchange quotations are by no means necessarily a reliable basis, if there be no free market. Again, it may be pointed out that, following the ordinary principles of the valuation of unsold stock, no appreciation in the value of investments ought to be credited to Revenue until those investments have been actually sold. It is not, however, necessary to write down each separate investment that has depreciated, while writing up those that have appreciated; the proper course would appear to be to maintain the investments in the Balance Sheet at cost price, making provision for a Reserve sufficient to cover any deficiency in the aggregate intrinsic value, as contrasted with the aggregate book value. Realised profits may, of course, be properly credited to Revenue; but care should be taken to see that they have been actually realised in cash, and, so far as possible, the Auditor should be upon his guard against the inflation of profits by means of “accommodation” transactions between different members of a group of companies. Probably the *Whitaker Wright* frauds will be sufficiently fresh in the minds of readers.

to make unnecessary any detailed explanation of what is alluded to under this heading.

To sum up, it appears that although, so far as the authorities have hitherto gone, it would appear that under some circumstances dividends may be legally declared out of current revenue without first making good depreciation of investments, it is, on the other hand, certain that the declaration of such dividends is a direct violation of every principle of sound finance, and should at all times be discouraged by the Auditor, who should make sure that the true position of affairs is sufficiently revealed to the shareholders, either upon the face of the accounts or by a special clause included in his report.

CHAPTER IV.

SPECIAL CONSIDERATIONS IN DIFFERENT CLASSES OF AUDITS.

(Continued.)

IV. GAS AND WATER ACCOUNTS.—(a) GAS COMPANIES.—It is not essential that a Gas Company be incorporated under special Act of Parliament; but, as it can by no other means obtain power to pull up roads for the purpose of laying down or taking up mains, &c., it is very unusual to find a company of any importance not so incorporated. In such cases, however, as do exist, the company is under no special statutory obligation with regard to its accounts; but in general respects the Auditor's duties will be the same as those of the Auditor of a company incorporated under a special Act.

In the case of a Gas Company especially incorporated, it is, of course, necessary that the Auditor should make himself thoroughly acquainted with the particular Special Act; in it he will find provisions as to share and loan capital, the rate of dividend or interest to be paid thereon, the standard price of gas, and other particulars which will have to be borne in mind. He will also find certain General Acts incorporated with the Special Act, and with these he must make himself thoroughly acquainted in so far as they affect his duties. Those sections of these Acts that refer immediately to the Auditor's duties or to the form of the accounts, will be found reprinted in Appendix "A."

The form of accounts given in Schedule B of the Gas Works Clauses Act 1871 applies to all companies whose Special Act incorporates either the 1871 Act, or the Gas Works Clauses Act 1847. The latter Act and its amendments also make provisions with regard to the formation of Reserve and Insurance Funds, and provide for the issue of new capital under what are known as the Auction Clauses. The appropriation of profits under the sliding scale is also introduced.

One of the most important matters, from the Auditor's point of view, is the division of all expenditure into two classes—Capital and Revenue. The wording of the statutory form of accounts will probably sufficiently indicate the basis of this division; it remains, therefore, to say that, perhaps, the Auditor's most important duty is to see that this basis is maintained. It is not, however, always possible for the Auditor to judge as to the correctness with which, say, the cost of an improvement, or renewal, has been apportioned as between Capital and Revenue; nor, indeed, is it necessary that he should so constitute himself an engineering expert. He will, however, require to see that the company's engineer has certified the apportionment to be correct, and that the expenditure on Capital Account has been passed by the Board. In addition, it is desirable that he should satisfy himself that the principle followed by the engineer in arriving at his apportionment is a sound one. There is, properly speaking, no "safe side" in these matters—an undue charge to Capital is unfair to the proprietors, while an undue charge to Revenue is (through the operation of the sliding scale) an injustice to the consumers. The following examples of apportionment will, however, be found useful, as indicating, in general terms, the correct method of arriving at the amount chargeable against Capital, and against Revenue, in any special case that may arise:—

NEW WORKS (including extensions): Capital.

NEW WORKS IN PLACE OF OLD WORKS: Charge original cost of old works pulled down, less value of old materials, against

Revenue ; charge the remainder against Capital. (This amounts to debiting Capital with total cost, debiting Revenue and crediting Capital with original cost of old works, and crediting Revenue with value of old materials sold.)

The above description accurately explains the theoretical apportionment of expenditure on renewals as between Capital and Revenue ; but, for practical purposes, it is important to bear in mind that the cost of any kind of constructive work does not remain constant over an extended period. Assuming it did remain constant, no modification of the principle already described would be necessary ; but, inasmuch as variations in cost are to be expected, it is important to bear in mind that only the *bonâ fide* "betterment" can be properly capitalised. Thus, if assets which originally cost £10,000 were, on renewal, to cost £12,000, the *whole* of the cost of such renewal would be a Revenue charge. If, however, the assets which originally cost £10,000 were replaced by assets of a higher revenue-earning capacity at a cost of £15,000, the correct method of apportioning this £15,000 would be to, in the first place, ascertain what the exact reinstatement of the original assets would have cost, to charge that sum to Revenue, and to only capitalise the excess.

There is reason to believe that in the past this rule has not always been applied with sufficient strictness to the expenditure of undertakings framed upon the Double Account System—whether Gas-works, Water-works, Railways, Tramways, or the like ; but there can be no question as to its soundness when the cost of constructive work is upon the increase. In new countries—as, for example, in most Colonies—the cost of constructive work has, owing to facilities for transport, been materially reduced of late, and thus the question arises as to whether the same principles may be fairly applied. If they were to be strictly applied, it is clear that pure renewal work, involving no "betterment" whatever, would indirectly result in a credit to Revenue, in that the original amount of Capital expended would be maintained in spite of the fact that Capital assets actually existing to represent it had cost less. Thus, an asset

which originally cost £10,000, and which was renewed (without detriment) at a cost of £8,000, would still be included in the Capital Expenditure at the former figure. This is, of course, the essential weakness of the Double Account System, if strictly applied: that, with reducing prices, its effect is to "water" the Capital of the undertaking. It is believed, however, that the usual practice under such circumstances is to depart from the strict principle of the Double Account System, and to write down the value of the Capital Expenditure as and when renewal work is undertaken at a reduced price, and this clearly is the only sound policy to adopt.

CONVERSIONS. In a similar case to the last—save that certain old materials, instead of being sold, are used for other purposes on the works—treat the particular department of Capital Expenditure as the purchaser of the old materials in question, debiting it with the value of the materials and the full cost of conversion (if any).

The income of a Gas Company consists of Gas Rates, Meter Rents, Residuals sold, and generally profit on Fittings and Rents, in addition to Transfer Fees and Interest on Investments. The collection of Gas Rates and Meter Rents are best checked in totals (in the manner shown under FIRE INSURANCE ACCOUNTS, care being taken to fully test both allowances and arrears), the total receivable being arrived at from the State of Meters Books, which will show the total amount of gas consumed and what meters are on hire. The residuals sold cannot well be checked as to quantity (save by comparing the results of various working statements), but, of course, the Auditor may, and should, check the collection of the amounts debited. The same remark applies to Fittings, which will almost invariably be found to form a part of a Gas Company's business, although no mention of the circumstances will be found in the statutory form of accounts. It may be added that it is best merely to state the profit arising from fittings on the credit side of the Revenue Account (rather than to credit Revenue with Income, and to debit it with Expenses), as there is nothing gained by showing

the whole world what percentage of profit has been made. The leading items of expenditure arise from Coal, Stores, and Wages; the latter has already been considered in Chapter I., and the former in Chapter II., and need no further consideration beyond saying that both must be fully vouched for, and carefully tested. All Cash Book entries must, of course, be vouched, the additions checked and the balance verified; also all the General Ledger postings should be called back.

Here—as in connection with all undertakings framed upon the Double Account System—it is important to bear in mind that the mere renewal of fixed assets as they become worn out will not of itself have the effect of maintaining Capital Expenditure intact, in that an appreciable interval of time (varying naturally according to circumstances) must necessarily occur between the actual deterioration in the value of an asset and the date when expenditure may be usefully and advantageously incurred upon renewal work. In the case of some undertakings—as, for example, Railways and Water-works—this discrepancy is not likely to have any serious bearing upon the accuracy of the accounts; but in the case of Gas-works (and to a far larger extent in the case of such undertakings as Electric-lighting Works and Tramways) the discrepancy is more marked; and with regard to these, unless some additional provision be made in advance, by way of a Reserve for future expenditure on renewals, the accounts during the earlier years of the undertaking will seriously exaggerate the true profits earned. The proper course to adopt under these circumstances would thus appear to be to set aside a sufficient sum annually to cover the average cost of renewals over an extended term, and to charge the actual expenditure in respect of renewals against the provision so created. In the case of Gas Companies this plan has to some extent been provided for by the Legislature, although probably unconsciously, and certainly unsystematically; yet there can be but little doubt that the statutory Reserved Fund and the statutory Insurance Fund were created to provide a sufficient Reserve to compensate for any inequalities that might be caused

by the strict application of the Double Account System to Gas-works. The absence of any such safeguard in connection with the more speculative undertakings already referred to is thus all the more notable.

The investments held against Reserve, Insurance, and (if any) Depreciation Funds, must be verified by an inspection of the securities held.

This leads up to the consideration of the Depreciation Fund (in reality a Sinking Fund), which must be accumulated by companies owning works on leasehold lands. The case will not often arise, but, when it does occur, a sufficient sum must be set aside, and invested to accumulate to the cost of the works by the time the lease expires. The Auditor will require to satisfy himself as to the sufficiency of the annual instalments.

It may be added that accounts have to be taken annually on the 31st December, and that a copy of the accounts must be filed with the prescribed local authority before the following 31st March.

Formerly, the Auditors of Gas Companies' Accounts were required to be shareholders, but in several recent Special Acts this qualification has been removed.

Metropolitan Gas Companies are subject to an official audit by the Board of Trade, but this does not prevent them from securing the advantages of a professional audit in addition.

MUNICIPAL AUTHORITIES are frequently empowered to trade in gas, but the consideration of these accounts is best deferred until the question of CORPORATION ACCOUNTS is reached (*vide* Chapter IV., section VI.).

(b) WATER COMPANIES.—The mode of audit best adapted to the accounts of Water Companies is practically identical with that which has just been considered. Some of the Acts there specified do not, however, apply to the undertakings of Water Companies; and, in particular, there is no

general statutory form of accounts. The Metropolis Water Act 1871 contains, however, some important provisions, which are included in Appendix "A." The water supply of London has now been placed under the control of the "Water Board."

It is a very general practice to assimilate the accounts of Water Companies, as near as may be, to the form laid down for Gas Companies in Schedule B of the Gas Works Clauses Act 1871—indeed, it is difficult to conceive a form better adapted for this purpose.

The audit of Water Companies is slightly simpler than that of Gas undertakings, by reason of the fact that the rates charged are, for the most part, fixed, instead of fluctuating with the quantity used. Such portion as is supplied by meter, for trade purposes, will entirely follow the method recorded under GAS COMPANIES. With regard to the greater portion, which is based on a sliding scale (for which see the Special Act) upon the rateable value of the houses, it is not usual to exhaustively check the calculations involved, but they should be *tested* to such extent as may appear desirable. Vacancies may sometimes be vouched by a declaration of the owner that the property in question has been vacant for the whole of the quarter. Allowances (which should be very exceptional) must be properly explained, while arrears and bad debts must both receive careful attention.

Most companies are empowered to make their rates in advance, and consequently their books will, at the date of the accounts, reveal a profit that has not yet been earned: due allowance must, of course, be made for this in the General Balance Sheet.

GAS AND WATER COMPANIES (COMBINED) will—in almost every instance—be found to be required by their Special Acts to keep the accounts of the two undertakings entirely separate. In the few old companies where no such provision exists, separate accounts should, at least, be made out for Capital Expenditure and Revenue (the management expenses being

apportioned according to, say, the ratio of the average gross income from each department), so that the profit upon each may be known and the proper working statistics prepared.

(c) **ELECTRIC LIGHTING ACCOUNTS.**—The statutes relating to Electric Lighting Accounts are the Electric Lighting Acts 1882 and 1888, together with the Board of Trade rules thereon. A concession (which, by the way, does not grant a monopoly) may be obtained either by a Special Act of Parliament, a Board of Trade Licence, or a Board of Trade Order, and may be granted to a private individual, a company (incorporated either under the Companies Acts or by a Special Act), or to a local authority. This concession lasts for 42 years, after which the local authority has the option of taking over the undertaking at the then value of its assets. There are no special provisions as to audit in the General Acts, it being left to the concessionaires to provide for audit as they may think best.

The Board of Trade have issued a special form of accounts: and accounts, drawn up in the prescribed form, are to be forwarded to the Board on or before the 31st March in each year, for the year ended the previous 31st December. The form now in use (which is shown in Appendix "A") is based upon that required from Gas Companies—the electricity being sold by the "unit," instead of by the thousand cubic feet.

The general method of audit will practically follow the lines indicated under the head of "Gas Accounts"; especial care should, however, be directed to the correct apportionment of expenditure between Capital and Revenue.

Electric Light Accounts differ from those of most other undertakings which are compiled upon the Double Account System, in that the perishable nature of the fixed assets renders it imperative that special attention should be devoted to the subject of Depreciation. It is not merely sufficient that the working plant should be fully maintained in a state of working efficiency out of Revenue, as the high speed at which the machinery is run,

combined with the fact that only the smallest possible intervals of rest can be afforded to rectify defects, very materially shortens the duration of the life of these assets. Moreover, in connection with this particular industry the advances of modern science are so rapid that, in spite of this comparatively short time of life, many parts of an electrical plant become obsolete before they are worn out. For these reasons a high rate of depreciation must be provided, and it is now being realised that in most cases depreciation has occurred at a more rapid rate than has been provided for in the accounts.

It is thought that a minimum safe provision against depreciation of the actual expenditure as a whole would be one equal to 4 per cent. on the total capital expenditure. It may be added that, of the two Municipal Corporations which appear to have been among the first to appreciate the importance of adequate provision for depreciation, Glasgow provides—on Machinery, $7\frac{1}{2}$ per cent.; Accumulators, 10 per cent.; Mains, $2\frac{1}{2}$ per cent.; Meters, 6 per cent.; Instruments, 5 per cent.: while Bolton writes $7\frac{1}{2}$ per cent. off Machinery, 20 per cent. off Accumulators, 10 per cent. off Mains, and 5 per cent. off Transformers. Speaking quite roughly, it may be said that the average working life of an electric lighting undertaking (*en bloc*) is usually about 40 years; but, in the nature of things, it varies greatly according to circumstances.

One caution in conclusion may not, however, be out of place: where no regular Bought Ledger exists—and this state of affairs will also be frequently found in connection with both Gas and Water Companies as well—particular care will be necessary to guard against any omission of outstanding liabilities, when the annual accounts are drawn up.

V. TRAFFIC ACCOUNTS.—(a) RAILWAYS.—In almost every instance Railway Companies are incorporated by Special Act of Parliament. Such companies are subject to the provisions of the Companies Clauses Act 1845, the Railway Companies Act 1867, and the Regulation of Railways Act 1868

(extracts from which will be found in Appendix "A"), in addition, of course, to the requirements of their own Special Acts. A few foreign and colonial railways have, however, been registered under the Companies Acts: in such cases, of course, the details of administration will follow the provisions of the Acts under which they are registered; but it will generally be found that the articles of association enable the accounts to be kept and audited in the same manner as those of companies registered under a Special Act of Parliament. Attention should be directed to any legislative requirements that may be operative in the country where the railway is situated.

The statutory form of the accounts (which are taken half-yearly) and the Auditor's certificate are to be found in Appendix "A"; it therefore remains to consider what the extent of the Auditor's investigation should be which will enable him to certify that the accounts are a "full and true statement of the financial condition of the company, and that the dividends proposed to be declared on the stock and shares of the company are *bonâ fide* due thereon, after charging the revenue of the half-year with all expenses which, in (our) judgment ought to be paid thereout."

The actual extent of the Auditor's responsibility is a matter of some little uncertainty, but it is at least certain that he is not to be held responsible for every detail of the half-year's recorded transactions. The audit of these details occupies the whole time of the Chief Accountant and the audit staff; and not only would it be a physical impossibility for the professional Auditor to go over the whole of their work, but it would also be a lamentable waste of time and money.

The Audit Office, in itself, constitutes a continuous and thorough check upon every other department under the supervision of the Accountant, and, as no moneys whatever pass through that office, it may safely be taken that the work is honestly performed.

The Auditor's work may thus be said to commence with the certified returns of traffic, and the certified accounts of tradesmen and others. He must, however, himself examine and verify the summaries of these items. He must see that they tally with the cash and bills received, and that the latter find their way into the bank in due course. He must examine the vouchers of all expenditure, and, so far as possible, verify its apportionment; in particular must he satisfy himself as to the correctness of the apportionment of such expenditure between Capital and Revenue. With regard to the issue of new capital, he must see that the amount actually received agrees with the totals shown in the Stock and Share Ledgers kept at the secretary's office. He should compare the certified returns of the Railway Clearing House and "Foreign" Railways with the entries in the books of his own company. He should check the transactions in bills in detail, follow the matured bills into the Banking Account, and verify the outstanding bills by the inspection of the actual documents. He must check the traffic outstandings with the certified statements, examine the entries on both sides of the Banking Account, and check the additions, and, so far as possible, the classification of the items. He should examine all debentures that have been redeemed, and see that they have been cancelled. He should examine the accounts for repairs done to the rolling stock of customers, and compare the lists with the Ledger. He should examine the accounts of rent received, thoroughly check the General Ledger, compare the balances of the various Stock Accounts with the certified list of stores on hand, compare the totals of the General Ledger Expenses Account with the totals of the subsidiary books. It will then still remain for him to ascertain that such liabilities as traffic drawbacks are provided for, verify the investments by inspection of securities and examination of the interest received, compare the capital issued with that authorised by Act of Parliament and shareholders' minutes, give a final consideration to the apportionment of Capital and Revenue Expenditure, and see that the necessary certificates have been furnished as to the efficiency of the permanent way, rolling-stock, &c.

Since the last edition of this work was published methods of Railway Accounting have attracted far more public attention and public criticism than was at one time the case. To some extent it seems not unlikely that these criticisms represented nothing more serious than a "bear" conspiracy to depreciate the value of railway securities, with a view to enhancing the profits of speculators; but, whatever may have been the origin of the movement, it no doubt attracted the attention of the public and of the thoughtful student of accounts, because it was put forward simultaneously with the announcement that certain railways were about to incur very considerable capital expenditure in the modernising of their equipment, and in the application of electric motive power to local traffic. Any such wholesale conversion as a change from steam to electric motive power naturally suggested that much of the original capital expenditure would, under the altered conditions, have to be set aside as useless; and whatever the Courts may have decided with regard to the allocation of such expenditure as between Capital and Revenue (upon which point the decision in *Cox v. The Edinburgh and District Tramways Co., Lim.*—*vide* Appendix "B"—may be usefully consulted), the fact must, of course, in all cases remain that expenditure upon abandoned works represents a LOSS, whether that loss be regarded as a loss of Capital or a loss of Revenue. The question was also raised as to whether in the past Railway Companies had in all cases applied the Double Account System sufficiently strictly, bearing in mind the fact that the cost of constructive work has increased very considerably of recent years. The point is one upon which it is manifestly impossible to usefully generalise; all that can be done in this work is, therefore, to draw attention to the dangers and difficulties suggested, but the following extract from *The Financial Times* of the 15th September 1902 will be found useful as summarising these difficulties, and therefore recapitulating the more important points that will require to be carefully considered in connection with every Railway Audit:—

"Various readers have addressed inquiries to us as to the methods adopted by our railways in regard to capital charges and how the line

is drawn between capital and revenue. No doubt the problem has presented itself to their minds in connection with the discussion now proceeding in regard to British railway finance and the adverse effect it has had on quotations. To begin with, we may explain that no item which is obviously a legitimate charge to revenue would be likely to be charged to capital—that is, if Auditors discharge their duties. They are required to certify that ‘the dividends proposed to be declared on the stocks and shares of the company are *bonâ fide* due thereon, after charging the revenue with all expenses which in our judgment ought to be paid thereout.’ That certificate is appended to all the half-yearly accounts, and so far as revenue is concerned ought to be conclusive. But it will be noted that it makes no reference to capital charges at all, except inferentially. All new lines, including land, buildings, and works, Parliamentary and legal expenses, are charged to capital. All the cost of maintaining the permanent-way, rolling-stock, stations, bridges, sidings, signal boxes, &c., in their original state of efficiency ought to be charged to revenue. If an engine, carriage, wagon, or any other equipment is worn out, the cost of replacing it goes to revenue. But if an addition is made to working stock of any kind it is generally—but not always—charged to capital. In fact, anything which is academically a fair charge to capital goes to that account. Suppose, for example, a new signal-box is put up in place of one destroyed, and the new one has cost double the original one, the extra cost is charged to capital. Similarly, if a big new station is put up in place of a smaller structure, the additional cost is charged to capital. So with rolling-stock. If electric fittings, for example, are put into an old train, the cost is charged to capital. The principle seems to be to maintain an even balance between the Capital and Revenue Accounts; but under any circumstances the dividend must not be allowed to suffer. An analysis of the capital expenditure of our railways shows that the bulk of it (about three-fourths) goes into the items of lines open for traffic and working stock, and only a small proportion into new lines. This explains the failure of additional mileage open to keep pace with the extra capital. Expenditure on lines open for traffic includes such items as widened lines, new stations, new sidings, extra carriage and locomotive sheds, extra over-bridges, larger signal-boxes, additional signals, and a host of other things which it may be argued are from an academic point of view quite legitimate charges to capital. But it seems to be overlooked that the criterion of value of an undertaking such as a railway is not the actual value of its property, but its profit earning power. Thus any charge to capital which does not add to profits and does not in any way contribute to increase earnings is not a charge to capital that can be prudently made. Take a new

station, for example, erected in place of an old one. In place of earning more revenue, it probably entails a larger staff, increased cost of lighting, and higher rates than the old one. This is a type of the unproductive expenditure which has been going on so long that it now represents an annual charge on the undertakings which they cannot shake off, and which gradually reduces the average net return on capital as a whole. If a railway company spends in the course of ten years, say, 10 millions sterling on such improvements, at the end of that time it has added £350,000 to £400,000 to the annual charges which must be met before profits are arrived at. If it had spent the same sums out of revenue, dividends would have been poorer during the ten years, but at the end of the period about £400,000 a year extra would be available for division. And it is hardly necessary to say that if revenue had had to be saddled with those charges, probably not nearly so much would actually have been spent, and five millions might have been made to go as far as ten millions. If Depreciation and Reserve Funds existed on a substantial scale, there would be less reason to find fault with unproductive capital outlays, which have to some extent been forced upon the companies to meet the requirements of the public and the traders without any *quid pro quo*. It is ridiculous to suppose that a great deal of the antiquated rolling-stock floating about the country, or that the permanent-way and stations in many cases, are maintained in their original efficiency. Of course, it is a matter of degree; some companies adopt a more liberal policy than others. But as a whole our railways have yet to learn that large unproductive capital outlay is unwise and short-sighted."

Hitherto a notoriously weak feature of Railway Accounting has been the absence of any *systematic code* for the allocation of all expenditure over the proper headings. Of late, however, this reproach has been removed in the case of the Great Northern Railways, and—it is believed—also in the case of the North-Eastern and the Great Western Railways.

(b) TRAMWAYS.—With the exception of the few tramway undertakings that are governed by the legislation affecting railways, there is no prescribed form in which the accounts of Tramway Companies are to be presented; considerable variations will therefore be found in the mode adopted by different companies.

The accounts are usually prepared upon the Double Account System—permanent way, rolling-stock, and horses constituting the items of Capital Expenditure. With regard to the first two items, on account of the extreme difficulty of making any periodical estimate of their value, the method adopted is, perhaps, the most convenient one—the work being maintained in a state of perpetual efficiency rather than reduced by depreciation and increased by renewals. As regards “Horses,” however, the unpermanent nature of this item appears—in spite of the fact that such a course is unusual—to lend itself more readily to the “Single Account” method of treatment—namely, by writing off depreciated value and debiting the account with fresh purchases. The certificates of the responsible officials must always be obtained for the efficiency of the assets represented by the Capital Expenditure.

The traffic receipts must be carefully tested, and it is not unusual for the Auditor to consider it necessary for him to go over the whole of this work in detail, commencing with the tickets, guards’ books, or way-bills (as the case may be), and tracing the receipts on to the traffic sheets and daily and monthly traffic books, and seeing that the whole amount received has been duly banked. Where the system employed does not provide a perfect internal check it would seem to be very desirable for the Auditor to examine every detail, for it is here, especially, that a leakage is likely to occur. It may, perhaps, seem superfluous to suggest the propriety of seeing that receipts are accounted for upon every day of the year.

The only other source of revenue of any importance will be advertising; but, as this is almost invariably sub-let to a contractor, it needs no comment.

The expenditure—which should always be made by cheque, no payment out of traffic receipts being on any account permitted—must be carefully vouched; while the analysis thereof must, so far as possible, be verified. In particular, the apportionment between Capital and Revenue must be thoroughly scrutinised.

The Horses Account is one that might easily be manipulated, and must be particularly watched; the number of horses shown on the account should, of course, agree with the number stated on the vet.'s certificate. With electric trams the question of depreciation becomes a very important one (*vide* p. 117).

Under modern conditions, however, the question of Tramway Accounts has to be considered not merely in connection with horse tramways, but also as applied to those with mechanical—and especially with electric—motive power. The difficulties of strictly applying the principles of the Double Account System to horse tramways have already been dealt with; but it should be borne in mind that these difficulties are by no means obviated by the adoption of steam, petrol, or electricity, as a means of locomotion. Tramways, however, represent a class of undertaking which is not really suited to the Double Account System, in that the mere repair and renewal of fixed assets as they become worn out will not, even approximately, charge a sufficient sum against Revenue to enable the true profit to be accurately determined. The difference between the deterioration in intrinsic value and the amount that can be usefully spent from year to year in repairs and renewals is very marked indeed; while the very short mileage of even the largest tramways, as contrasted with a railway, further aggravates the deficiencies of the Double Account System.

These points are beyond the stage of mere discussion, in that the existence of depreciation as an important factor in connection with Tramway Accounts is admitted not merely by accountants, but also by tramway men; and all successful tramway undertakings make substantial provision for Depreciation, in addition to charging Revenue with repairs and renewals. It may be added that, at a recent conference of Tramway Managers at Glasgow, a form of accounts providing for Depreciation to be actually deducted from Capital Expenditure was agreed to. Inasmuch as the essence of the Double Account System is to perpetually maintain Capital Expenditure at its original value (making in exceptional cases a Reserve, *per contra*,

for deterioration), it will be seen that this resolution, to the effect that it is desirable that Depreciation should be deducted from Capital Expenditure, is tantamount to an admission that the Double Account System is unsuitable to these undertakings, and to a reversion to the Single Account System. The exact form of the accounts is, however, of course not material, so long as the actual deterioration in value is (in one way or another) charged against profits, so that the balance of the Revenue Account may not show a figure in excess of the true working profit of the undertaking.

In this connection it is of interest to note that the Subcommittee appointed by the Institute of Municipal Treasurers and Accountants to attend the joint-conference with representatives of the Municipal Tramways Association, has issued an interim report on the question of Depreciation, from which the following is extracted :—

“Permanent Way Renewal—Depreciation.”

“It is felt that diversity of practice will inevitably take place with regard to the treatment of these two headings, and that it is impossible to attempt to lay down any binding principle on the corporations concerned as to what they should or should not do in these matters.

“Municipalities at the present time are, generally speaking, under an obligation to repay loans over a period supposed to represent the equated lives of the respective parts of a tramway undertaking, and much divergence of opinion exists as to the necessity or desirability of charging against revenue depreciation in addition to loan repayment or Sinking Fund.

“The question of depreciation in relation to the repayment of loan is an important one, not only in connection with tramways, but also in respect of electricity undertakings, and as a good deal has been said on the subject by persons interested in criticising the financial administration of municipalities, it may not be out of place to briefly record the actual position of such authorities in these matters.

“The great loan sanctioning department of the State is the Local Government Board, which grants loans under the Public Health Acts, Electric Lighting Acts, Municipal Corporations Act, &c.

"Under the Public Health Act, the expression relating to borrowing money is 'for permanent works (including any works of which the cost ought, in the opinion of the 'Local Government Board, to be spread over a term of years),' and under the Municipal Corporations Act, for the purchase of land or for the building of any building.'

"Loans for tramway purposes are sanctioned by the Board of Trade under the Tramways Act 1870, 'for expenses in applying for and obtaining the Provisional Order and carrying into effect the purposes of such Provisional Order.'

"It has been the invariable rule of the State Departments to sanction separate loans for periods which they believe, as a result of their experience, to be commensurate with the lives of the undertakings, such lives being regarded as rarely exceeding a generation of 30 years.

"Where, however, an undertaking consists of several component parts, the respective lives of which would vary, the departments have, in many instances, given a period which would be equal to the equated lives of the aggregate sections.

"There is nothing in law to prohibit the departments from sanctioning a loan for the *renewal of an undertaking or work a second time, provided that no part of the previous loan remains outstanding.*

"It has been stated by persons presuming to know something about public finance that the *intention* of Parliament in framing the Acts referred to, was that when once a loan had been granted it should never be renewed for the same purpose. The practice of the Local Government Board has, however, been to the contrary, and it is submitted with confidence that, if an authority chooses to apply for a fresh loan for the renewal of a work in respect of which the original loan has been redeemed, all other statutory conditions being equal (*e.g.*, limitation of borrowing powers, &c.), there would be no valid reason why the department—if, indeed, it were able—should refuse a loan for renewing such work.

"Obviously no hard and fast rule can ever be laid down in this respect, as it would bring local government in many cases to a standstill if authorities were compelled to provide the wherewithal to renew the undertaking at the termination of its life, in addition to redeeming the cost of the original construction.

"Whilst, therefore, local authorities have the power to borrow for the purposes of the statutes which they carry out, the Sub-Committee do not feel that they are called upon to make any definite proposal in

regard to a policy which would have the general effect of imposing an obligation which in law does not exist.

"Considerable misapprehension appears to have arisen in the public mind as to whether local authorities really do repay by Sinking Fund or otherwise the loans incurred by them, and the question of providing depreciation appears to have been confused in the issue, generally speaking due to the fact that in many cases one loan has been granted for a period representing the equated lives of the various sections of an undertaking.

"Assuming that separate loans were granted for each section over periods representing as nearly as science and experience can determine the life of an object, it is perfectly clear than when a loan has been repaid no actual deficiency exists against the local authority, and it is at liberty to reborrow if necessary. In practice this is rarely done at the time, as the work has been kept in an efficient state by constant repairs, so that the life is usually extended far beyond the original period sanctioned.

"When, however, one loan is granted for a period representing the equated life of the whole of the sections there certainly is a danger, unless great care is exercised, that the repayment of the loan in the earlier years of the period would not adequately protect the authority in the sense of enabling it to reborrow for those works or parts thereof the life of which was less than the *average* life of the undertaking—*i.e.*, less than the equated period.

"In repaying a loan over an equated period, the local authority has the advantage of distributing the capital charges equally over the whole period, whereas if separate loans had been granted the repayment of those representing the short-lived works would fall heavily upon the undertaking in its early years.

"Before the expiration of the period of an equated loan, occasion may, and theoretically must, arise for renewing short-lived works, and it is precisely at this point that the danger lies of an authority finding itself unable to renew owing to the fact that it cannot reborrow because the loan has not been wholly repaid.

"Provision should therefore be made annually to meet this risk, and it is suggested that each authority should, as a result of its experience, charge a sum for adequate renewals (*i.e.*, depreciation) of wasting assets by creating special funds for this purpose, but reserving to itself the right, if it thinks fit, of paying thereout the Sinking Fund or loan repayment charges. This suggestion would involve a consequential

modification of the net Revenue Account as shown in the suggested form.

"It should be clearly understood that the Committee do not suggest that a local authority should not pay both loan repayment and depreciation charges out of the revenue of its undertakings if it thinks fit, as in many cases this may be quite possible, and under any circumstances would be a wise and prudent course to adopt.

"The Sub-Committee, however, is sensible of the fact that it is impossible to lay down a hard and fast line of this character, as local circumstances vary so greatly that whilst one authority would be perfectly justified in charging both items, another could not do so without inflicting an intolerable burden upon the present generation of ratepayers."

Tramway statistics for short periods will be of but little value to the Auditor as a general check upon the satisfactoriness of affairs; but statistics of longer periods may prove most useful, if intelligently applied.

(c) SHIPPING COMPANIES.—Unlike the accounts of Railways, the accounts connected with marine traffic are subject to no special statutory provisions with regard to form.

There is no essential difficulty in connection with Shipping Accounts, but the fact that it is both desirable and customary to show the net result of every voyage of every ship necessitates some very nice apportionment of the items constituting Shore Expenses and Insurance.

The extent of an Auditor's investigations will vary greatly in different cases: in the case of a Single Ship it is desirable that the audit be as exhaustive as possible; but in the case of one of the larger Companies such a course would be quite as impracticable as in the case of a Railway. The actual extent in any particular case will thus be very largely a matter of arrangement and of expediency.

The following considerations may, however, be safely submitted, as they will in every case require to be dealt with in more or less detail.

Ascertain that freights and passage money are duly accounted for ; that the apportionment of shore expenses is equitable : that the Cost Accounts are not improperly manipulated (especial care being required where one Cost Account is kept for a whole fleet) ; that only structural improvements are debited to Cost Account ; that proper depreciation is allowed—especially in regard to boilers ; that outstanding freights and agents' balances are provided for in accordance with the documentary evidence ; that unclaimed return passages are in order ; that proper return of insurance premiums has been obtained for the time during which any vessel has been "laid up," and, generally, that insurance matters are in order ; that the question of foreign exchanges has been dealt with upon a proper basis ; and that no profits are taken credit for on account of uncompleted voyages.

In order to prevent misunderstanding, it seems desirable to point out, for the benefit of the reader who has no experience of Shipping Accounts, that the "Cost Account" is really neither more nor less than a Capital Expenditure Account, and must on no account be confused with the Cost Accounts kept by manufacturers.

Some shipowners, instead of insuring with underwriters against risk of total loss or damage to their vessels, raise an Insurance Fund wherewith to meet such losses by periodical charges against Revenue. The effect, of course, is that, instead of Profit and Loss being debited with insurance premiums, it is debited with an instalment—probably somewhat in excess of that which would have been thus paid—which is credited to the Insurance Fund. At the same time, to make the Insurance Fund really effective when required, it is desirable that a corresponding amount of cash should be invested in readily realisable securities, the Insurance Fund thus becoming for all practical purposes a Sinking Fund, rather than a mere reserve. When any loss is incurred, the cost of replacing it is debited to the Insurance Fund Account, a corresponding amount of investments being realised to provide the necessary cash. It need

hardly be pointed out that an Insurance Fund can only become an effective provision against loss in the case of companies owning a large fleet of vessels, so that within their own experience they get a reasonable average of risk. Even here, however, it will sometimes happen that a loss occurs which will more than swallow up the whole of the accumulated fund, and the question then arises whether it is reasonable to bring forward the *debit* balance of the Insurance Fund Account as an asset upon the Balance Sheet. If there is a reasonable probability that this debit balance can be extinguished out of future instalments within a short time, there is probably no objection to this course of procedure; but, in any event, it seems desirable that it should appear as a special item in the Balance Sheet, so that no shareholder may be deceived as to the actual position of affairs; and, in addition, the Auditor would do no harm by drawing attention to the facts in his report.

OWNERS OF SINGLE SHIPS and SINGLE-SHIP COMPANIES almost invariably make no provision for depreciation: the Auditor need not waste his time upon any efforts to convince his clients of the imprudence of this course, but he should not forget to append the necessary qualification to his report.

The Auditor of Single-Ship Companies must bear in mind that, as regards fraud, there is no such thing as "safety in numbers" here, for the accounts are usually all in one person's hands—let him, therefore, not omit to examine the Voyage Account Book in detail. In a case decided a few years since it transpired that the same manager had control of the funds of several Single-Ship Companies; and, by an ingenious process of "ringing the changes," was enabled for many years to conceal from the Auditors the fact that there were serious deficiencies in his Cash Balance.

It is a good plan always to ascertain that no mortgage has been registered against the ship which is not recorded in the books.

VI. ACCOUNTS OF LOCAL AUTHORITIES.—The accounts of local authorities, and their audit, are subject to the provisions of numerous statutes; the principal Acts being the Municipal Corporations Act 1882 (for the accounts of the Borough Fund), the Public Health Act 1875 (for the accounts of Sanitary Authorities), the Local Government Act 1888 (for the accounts of County Councils), the Local Government Act 1894 (for the accounts of Parish Councils), and the Local Government Act 1899 (for the accounts of District Councils), in addition to such Special Acts as may have been obtained. In Appendix "A" will be found extracts from such portions of the General Acts as are of professional interest.

For some reason best known to the Legislature there is no statutory form for the accounts of the Borough Fund, but a return of "Receipts and Expenditure" must be made annually to the Local Government Board. The term "Receipts and Expenditure" is, of course, in itself—from an accountant's point of view—entirely meaningless, and it is generally understood that the account required by the Legislature is an Account of Receipts and Payments (or Cash Account). Every consideration of convenience, however, points to the desirability of all local authorities submitting their accounts in the form of an Income and Expenditure (or Revenue) Account, so that the actual financial result of each year may be clearly comprehended. The result is that many local authorities prepare and publish accounts which do not have to be—and probably are not—submitted to the Local Government Board for their approval; but it is understood that in some cases the actual Revenue Account has been filed instead of the prescribed Cash Account, and that it has been accepted.

Accountants will sometimes find themselves in the position of Elective Auditor, but, generally, their appointment will be held independently of, and in addition to, the elective audit and direct from the Corporation. At one time it was thought that the duties of Elective Auditors were strictly limited to a verification of the Treasurer's Account of Receipts and

Payments. The statutory rights afforded to Elective Auditors would certainly appear to have been framed upon a very restricted view of what such officers were expected to perform; but the decision of the Court of Appeal in *Thomas v. Devonport Corporation* goes a good deal further, and makes it clear that anyone holding the position of "Auditor" is entitled to perform a reasonable audit. It is thought that an Elective Auditor has a perfect right to report to the ratepayers direct: but as a matter of expediency it is suggested that he should not do so, unless the Council omit to publish his report, or delay doing so for an unreasonable time.

The duties and responsibilities of a professional Auditor would be determined by the terms of his appointment. His clients are the Council, and he cannot exceed their instructions.

The accounts must be made up and audited half-yearly, and printed and published annually, within one month of the close of the financial year. Both on account of the shortness of the time thus allowed for audit, as also upon more general considerations, it is, however, both advantageous and usual for the professional audit to be a continuous one.

The Accounts of the Sanitary Authority are upon the form settled by the Local Government Board. Where the authority is not also the council of the borough, the audit devolves upon the District Auditor, who is an official nominated by the Local Government Board; but where the Sanitary Authority is also a borough council, the accounts are audited by the Auditors of the Borough Fund.

It is the opinion of most experienced Auditors that no efficient audit can be made without an exhaustive examination into every detail, for the transactions of local authorities are so numerous and various that it is impossible to take a bird's-eye view of the matter. Thus the late Mr. WM. EDMONDS, F.C.A., F.S.S., in a lecture upon "Corporation Accounts," has said, "In my experience it is the smaller items of receipts and payments that generally are the most fruitful source of

defalcations and irregularities. Non-professional Auditors would pass over much detail, and are frequently content to merely cast the Cash Account submitted by the Treasurer, considering such to be their sole duty." (*See also a few paragraphs further on.*)

The Sinking Fund instalments must in all cases receive the Auditor's close attention : he must satisfy himself as to their sufficiency for the redemption of the loans within the periods prescribed ; and verify the investments of the fund, both as to principal and interest.

The actual significance of a Sinking Fund and the method of dealing with it in the books of a Corporation are not always so well understood as might reasonably have been expected. A Sinking Fund is created by periodically debiting instalments against Revenue, and crediting the amount of such instalments to Sinking Fund Account. A corresponding amount of Cash is simultaneously set aside and invested, the interest as received being credited to a Sinking Fund Account and reinvested. The instalments chargeable against Revenue are so based that, by the time the Loan in respect of which the fund has been created is redeemable, a corresponding amount of investments are available for its repayment. Upon the Loan being repaid the Sinking Fund ceases to be a Sinking Fund proper, and becomes a Reserve Fund or an accumulated Surplus. In practice it is not usual to keep a separate Sinking Fund Account in respect of each Loan, but it is important to ascertain that the instalments set aside will duly accumulate to the required amount. Subject to certain restrictions, a Corporation is entitled to invest its Sinking Fund instalments in its own Stock.

With regard to the routine to be adopted in any particular case, much will naturally depend upon the individual circumstances ; but the best plan will be to reproduce here the "Instructions" prepared by the late Mr. F. R. GODDARD, F.C.A., for the audit of the Newcastle-on-Tyne Corporation Accounts. The standard set up is, doubtless, a very high one,

but it cannot be considered to involve anything beyond the strictest necessities. The late Mr. WM. EDMONDS, F.C.A., when speaking of these *pro formâ* instructions, said "In my opinion there is nothing superfluous contained in the lengthy detail set forth by Mr. GODDARD: for myself, I have found it absolutely necessary to check every penny of receipts and payments before I sign the accounts."

INSTRUCTIONS FOR AUDIT.

As revised at 10th March 1887.

MONTHLY AUDIT.

TREASURY DEPARTMENT.

Cash Receipts Pass Books.—Check additions of all Pass Books, and see that total receipts are signed for by Treasurer, and entered in Treasurer's or General Cash Books. See that the head of each Department signs the Pass Book of his Department weekly.

<i>Departmental Pass Books—</i>	<i>No. of Books.</i>
Package Dues	}
Cranage Dues	
Port and Harbour	
New Streets Formation	}
Materials Sold	
Manure Sold	
Work Done	
Old Materials	
Fever Hospital	}
Rents	
Rates	

Collectors' Pass Books and Cash Books.—Check Debits of Pass Books with Collectors' Cash Books. See that the Collectors' Pass and Cash Books are initialled by Treasury Clerks. Check counterfoils, Collectors' Receipt Books, with their Cash Books, for two or three weeks in each half-year. See that Collectors sign their Pass Books and Cash Books weekly:—

Cattle Market (4), Cattle Market (Accommodation Pens, Corn Market), Concert Hall, Cattle Sanatorium, Concerts, Hirings, Thorough Toll, Butcher Market and Vegetable Market, High Bridge Female Lavatory, Elswick Park (3), Armstrong Park (3), Brandling Park (3), Leazes Park (3), Sandhill Weigh House, Refunded Workmen's Wages.

Miscellaneous Pass Books.—See that Pass Books are initialled by Treasurers' Clerks. Check occasional Counterfoils with Pass Books.

Baths and Wash-houses.—Check Daily Statements to Pass Book, and see that former are signed by Cashier and Superintendent.

Weights and Measures.—Check occasional Counterfoils with Inspector's Cash Book.

St. Mary's School.—Check a few entries in register occasionally.

Hay Market Weighage and Standage.—Check occasional Counterfoils.

Chimney Sweep Certificates.—Check Counterfoil Receipt Book.

Pedlars' Certificates.—Check Counterfoil Receipt Book, Cabmen's Badges, Science and Art Class (Public Library).

Public Library.—Check Vouchers at Library occasionally with Librarian's Cash Book.

Royal Grammar School.—Check Counterfoils for pupils' fees to Cash Book.

Town Hall Rentals (Meetings, &c.).—Check Counterfoils and Diary occasionally.

Organ Performances— do.

City Concerts— do.

Freemen's Admission Fees.—Check Fees received with Freemen's Admission Book in Town Clerk's Office, Moor Small-Pox Hospital (Dripping Sold), Leazes Park (Skating), Recreation Ground (Skating).

Lough and Noble Models (Elswick Park).—Stick and Umbrella Receipts; check occasional Counterfoils, Gas Meter Book.

Treasury Receipt Books.—Check all Counterfoil Receipts given by Treasurer to Treasurer's Cash Book. Check all Day Book entries with Council Minutes, Police Pay Bills, Cattle Inspector's Sheets, and all other sources of information, and see that the correct amounts are carried into the books. Cattle Sanatorium (Standages).

Thorough Toll Compositions.—North-Eastern and North British Railways.

Fire Brigade Expenses.—Proportion charged to Insurance Companies: Call Fire Bills to Fire Brigade Day Book.

Services of Police at Factories.—Check vouchers to accounts and check additions of latter.

Town Hall Concert Room.—Letting of Hall, Organ, &c.

Hospitals.—Funeral Allowances Repaid.

Criminal Prosecutions.—Magistrates' Clerk's Fees, Police Superannuation Fund (as per Police Pay Bills).

New Road Baths (Rent from Lessee), Gallowgate Baths (Rent from Lessee), Northumberland Baths (Rent from Lessee), Home for Incurables (Garden Rent), Explosive Licences (issued by Town Improvement Committee), Freeman's Admission (fees to Treasurer), Cemetery Company (Dividends on Shares), Scotswood Bridge Company (Dividends on Shares), Old Horses sold, Quay Shed Rents (List from Quaymaster weekly, not included in General Rents), Tramways (Lessees' Rent), R. Thompson's Bequest Fund (Loans Repaid), Sir T. White's Bequest Fund (Loans Repaid), Education Rate (Precepts on Overseers), Gaol Rate (Precepts on Overseers), Town Moor Intakes (collected for Freeman), Slaughter Houses Licences, Deposit Tickets (Rubbish), Virgin Mary Hospital (contribution to Grammar and St. Mary's Schools), Library Rate by (Precept on Overseers), Lunatic Asylum (Mr. Pace, Treasurer, separate Cash Book).

Miscellaneous Receipts (Interest, &c.).—See that all Dividends and Interest on Funds invested for the year are received and entered in Cash Book.

Police Superannuation Fund, Dale Scholarship, Meikle Scholarship.—Interest Forms, Transfers by Cheque. Interest on Coal Dues, Money, &c. Receipts given on Receipt Forms, Transfers by Cheque.

H.M. Treasury.—Police Claims, Criminal Prosecutions, use of Police Van. Receipts on Special Forms supplied by Government.

Magdalene Hospital.—Dividends on Consols per Bankers.

School Grants.—Per Bankers on Government Forms.

Property Sold and Enfranchised.—Per Order of Council and by Deed enrolled.

Town Moor Purchase Account and Tyne Bridge Trust Fund.—Dividends on Consols.

Corporation 3½% Stock.—Check Stock Bank Book with General Cash Books.

CASH PAYMENTS.

Voucher Guard Book.—Call Vouchers and Wages Sheets to General Cash Books, stamping each voucher, and taking out a list of missing

vouchers in the Note Book. Bonds paid off and Conveyances of Property purchased to be produced as Vouchers. See that all Bonds paid off are properly discharged. See that Wages Sheets are signed by City Engineer and Surveyor.

Watching—Police Pay Bills.—Call Pay Sheets to Cash, checking separate Pay Sheets to total sheets.

Bank Pass Book.—Call Bank Pass Book to General Cash Books and check last Reconciliation, showing cheques outstanding and in hands of Treasurer at date, checking those in hands of Treasurer with Counterfoil Cheque Books.

Treasurer's Petty Cash Book.—Check additions, and see that there is £150 in hand. Count Cash in hand half-yearly, after giving credit for sums paid after last meeting of Committee.

Treasurer's Cash Book.—Check credits to debit of General Cash Books. Check additions.

General Cash Books (3).—Check additions.

Reconciliation of Payments with Committee Minutes.—Check total payments in Cash Books to monthly Reconciliation. Check Finance and all other Committee Minute Books to Book containing record of all cheques drawn, and see that the total payments in the Cash Book agree with total amount of cheques drawn during the month, excepting cheques in the hands of Treasurer, which have not been entered in Cash Book nor paid away at that date, which must be produced to the Auditors.

DEPARTMENTAL MONTHLY AUDIT.

TOWN IMPROVEMENT DEPARTMENT.

New Streets Formation.—Cash Book. Check all Counterfoils of Receipt Books for Cash received at the Office, and also all Counterfoils of Collector's Receipt Books to Cash Books. Check Receipts in Cash Book to Treasurer's Pass Book.

Rate Department.—Check a few entries here and there in Collector's Cash Books to Treasurer's Pass Book. See that Clerk from Treasury Office initials the Collector's Cash Books as having been checked by him.

General Rents Cash Book.—Check additions of Cash Book.

St. Mary Magdalene Cash Book.—Check additions of Cash Book.

Package Dues Department.—Check all Counterfoil Receipts from Merchants and Wharfingers (2 Books) with Cash Book. Verify any exceptional allowances with documents relating thereto. Call Counterfoil Receipts for commissions to Wharfingers' Book and check additions. Call Cash to Pass Book and check additions.

Port and Harbour Dues.—Call Counterfoils, Quaymaster's Receipt Book to Cash Book, Cash Book to Pass Book, and check additions.

Cranage Dues.—Check Counterfoils to Pass Book, thence to Cash Book, and check additions.

HALF-YEARLY AUDIT.

TOWN IMPROVEMENT DEPARTMENT

New Streets Formation.—Cash. Call all work charged during the period under audit from the Minutes and Estimates to the Day Book. Call Cash Book, Day Book, and Allowances Book to Ledger. Check additions of all books and extraction of balances half-yearly, proving their accuracy by totals. Examine arrears and take particulars of different classes of same yearly.

Old Materials Sold.—Check Book in Surveyor's Office with Invoices. Call Day Book and Cash Book to Ledger and check all additions. Check and prove balances and note arrears.

Manure.—Check yard sheets with Day Book in Surveyor's Office, one here and there as a test. See that all allowances are duly authorised by Committee. Call Day Book, Cash Book, and Allowance Book to Ledger. Check all additions and extraction of balances and prove same by totals in Reconciliation. Note arrears yearly.

Work done and Materials Sold.—Check occasional entries in Time and Material Sheets to test correctness of Day Book entries. Call Day Book, Cash Book, and Allowance Book to Ledger. Check all additions, prove balances, and note arrears.

Fever Hospital.—Check Register with Admission and Discharge Books. Call Register to Day Book, Day Book and Cash Book to Ledger. Prove balances and check all additions.

Rate Department.—Check rates made with Council Minutes, and see that Rate Books are signed by the Mayor and Town Clerk with Corporation Seal affixed. Call Counterfoil Receipts which have not been used to Irrecoverable Arrears Column in the Rate Books, and note any arrears written off for which no cancelled receipt is produced. Check additions (1 in every 3 pages). Check summaries, and see that the total cash received has been paid over to the Treasurer. Check General Summary in All Saints' Book, and also half-yearly Statement prepared by Mr. Pybus.

RENTS DEPARTMENT.

Rent Rolls.—Check occasional counterfoils for General Rents, and examine a few Tenants' Rent Books and Collectors' Collecting Books for

Tenement and Market Rent by way of test each half-year. Check one week's receipts each half-year, and see that the total rents received agree with the total cash paid over to Treasurer during that week. Check Council Minute Book, Engineer's Tenancy Book, Seal Book, Assignment Book, and Treasury Minute Book to Rent Minute Book and Day Book, to ascertain any alteration for General and Magdalene Rents. Call all entries in Rents Minute Book and Day Book to Rent Rolls as follows:—General Rent Roll, Magdalene Rent Roll, Tenement Rent Roll, Willington Tenement Rent Roll, Butcher Market Rent Roll. Check New Rent Rolls each year with that of previous year, and see that all alterations to close of preceding year are made in new Rent Roll. Check additions and Reconciliation in General Rent Roll. Check additions of all Rent Rolls, prove Summaries, and check same to General Rent Roll Reconciliation.

General Rents Cash Book.—Check receipts to Tenant's Pass Book. Check additions of Cash Book. Check Summary of Cash to Reconciliation in General Ledger and Enfranchisement Sales Ledger.

General Rents Ledger and Liberties Ledger.—Check half-year's rents charged to tenants, and see that all differences agree with Minute Books and Day Books. Check the following books with Ledgers:—Empties Book, Rates and Taxes Book, Arrears Book, Balance Book (yearly). Check additions of these books and totals to Reconciliation at end of General Ledger.

St. Mary Magdalene Cash Book.—Check receipts to Pass Book, and check Summary to Reconciliations in General Ledger and Enfranchisement Sales Ledger.

St. Mary Magdalene Rent Ledger.—Check half-year's rents charged to tenants, and see that all differences agree with Minute Books and Day Books. Check the following Books with Ledgers:—Empties Book, Rates and Taxes Book, Arrears Book, Balance Book (yearly). Check additions of these Books and totals to Reconciliation at end of General Ledger.

Enfranchisement and Sales Ledger.—Check interest for half-year, and check balances, arrears, rates and taxes, and carry to Reconciliation at end of Ledger.

Paving and Flagging Ledger.—Check half-year's charge and check balances.

PACKAGE DUES DEPARTMENT.

Check Register of Vessels arriving and sailing to Declarations of Cargo. Call Declarations of Cargo (see that Manifests are signed) to

Manifest Summary, and check Manifest Summary additions. Call Cash Book, Allowance Book, and Commission Book to Ledger and check additions. Call Ledger to Balance Book, check additions of latter, and prove total amount of balance by totals of the various books, as shown in the Reconciliation Statement; make copy of Reconciliation. Check transfers from Mr. Pace's Cash Book to Mr. Harvey's Petty Cash Book, and check additions of Petty Cash Book. Check transfers from Petty Cash Book to Stamp Book, and check additions of Stamp Book.

PORT AND HARBOUR DUES.

(Rent of Goods impounded by Quaymaster.)

Call Cash Book and Day Book to Ledger. Check additions of Ledger and check Balances to Balance Book. Check the Quaymaster's record of Goods impounded daily with the Day Book.

CRANAGE DUES.

Check sheets certified by Mr. Laws to Day Book. Call Day Book to Journal, Journal to Ledger, Cash to Ledger, Call Allowance Book to Ledger, and check additions of all Books. Call Ledger balances to Balance Book. Check Balance Book additions.

TOWN CLERK'S OFFICE.

Check Vouchers and all Deeds, &c., for Stamps charged into Cash Book, and make a note of any missing. Check from Counterfoil Receipt Book and Bills of Cost Book to debit of Cash. Check Sales of Parliamentary and Municipal Registers with Counterfoils, Fees on Leases for 75 years with Seal Book, Fees for Bonds under Thompson and White's Bequests with Loans granted, Fees for Freemen's Certificates of Birth with Guild Book, Fees for affixing Mayor's Seal to Affidavits and Foreign Documents with Register of same, and Fees for Freemen's Admissions to Freemen's Admission Minute Book. See that total receipts and payments agree with transfers in general Books.

MAGISTRATES' CLERK'S OFFICE.

(This Audit to be done on Wednesdays.) Check Rough Cash Book to Cash Book of Apportionment, and check latter to Daily Summary Book and that to Monthly Summary Book signed by the clerk. Check Vouchers of payments to Treasurer, and see that same agree with Magistrates' Clerk's Monthly total. Check additions of all Cash Books.

COUNCIL MINUTES.

Finance Committee Minutes.—Read through Council Minutes, checking into Seal Book all Bonds, Mortgages, Assignments, &c., and taking notes of all Cash transactions passed by the Council, and extract all Minutes relating to Special Grants and payments, increase in Salaries, &c., from Council and Finance Committee Minutes; also Town Improvement, Watch, Sanitary, Town Moor Management, Schools and Charities, Public Libraries, and Parks Committee Minutes. See that Council and Committee Minute Books are signed by Mayor and Chairman of Committees respectively.

Seal Book.—Check with and from Council Minute Book all entries in Seal Book, Call to General Rents and Magdalene Hospital Rents Day Book all new Leases, Assignments, &c., also to Bond Book and Stock Registers, New Loans to the Corporation, ticking the latter to the left of the amount.

STOCK REGISTERS.

Redeemable, Irredeemable, Holder, Bearer.—Check money paid from Cash Book, ticking to the right of the amount. Check Duplicate Stock Certificates issued to Stock Registers. Check Transfer Deeds to Transfer Registers and call latter to Stock Registers, and check total of Ledger balances to Summary. Check all Certificates issued to Council Minutes and Seal Book. Check balances of Stock Ledger to List of Stockholders, and see that total agrees with Summaries of Stock Registers at 25th March (yearly).

Bond Book.—Check with Cash Book the Cash received for new Loans, ticking to the right of the amount. Check Loan repayments into Cash Book and compare same with yearly Ledger, and see that the correct balance is brought down and carried forward each year.

LEDGERS.

Capital and Special, General Rate, City Fund, Intermediate and Trust Accounts.—Call Cash and Transfer Journal Posting and check additions. Check balances at 29th September and 25th March.

Treasury and Bequest Ledger.—Call postings of Treasury Cash Book, Miscellaneous Day Book, Sanatorium Day Book, Allowances and Fire Brigade Day Books to Treasury, and Bequest Ledgers (Thompson and White). Check all additions and extraction of balances. Check Summary of Cash Receipts and Payments and Cash Balances at 29th September and 25th March.

Outstanding Accounts and Allowances in Treasurer's and New Streets Departments.—Check half-yearly Statement of Accounts and Arrear Book (2).

Note.—Chief Clerk to examine all Pass Books and Collectors' Cash Books at the close of half-year, and see that they have been checked and initialled by Treasury Clerks, and that the Audit Instructions have been properly carried out in each case. Chief Clerk to initial each Pass Book and Cash Book, with date when examined by him.

YEARLY.

St. Mary Magdalene Hospital, Cash Book.—Check additions and see that total agrees with Balance Account in Ledger.

Package Dues, Cash Book.—As above.

Public Libraries, Ledger and Cash Book.—As above.

Lunatic Asylum.—Check balance forward from previous year. Check amount receivable for the year current from the Precepts and Minute Book. Check amount received from the Counterfoil Receipt Book. Check Bank Account, vouch all payments. Check balance forward and all additions.

Securities for Invested Funds.—Check Securities in hands of Town Clerk and Treasurer.

Accountant's Department.—Check Statement of Assets and Liabilities with Ledger. Check Redemption of Stock, Borrowed Money, Borrowing Powers.

During the past few years the attention of accountants and others has been specially directed towards the question of Local Authorities' Accounts, and the general financial policy of these bodies. This subject is thus of far greater importance at the present time than when the earlier editions of this work were issued. At this time of writing, the system on which the accounts of Local Authorities in England and Wales are at present kept, and the desirability of laying down further regulations with regard to the matter, are still the subject of inquiry by a Departmental Committee appointed by the President of the Local Government Board in January 1906. Pending the Report of that Committee, it is thought that the

matter can be most conveniently dealt with in this work by reproducing in full the following memorandum prepared by the author for the use of that Committee's Chairman :—

1.—The accounts of Local Authorities should be framed so as to meet the following requirements :—

- (1) To supply such information as may be necessary to enable the officials to see that all moneys receivable are duly received, and that no accounts are inadvertently paid twice over.
- (2) To enable a proper system of supervision to be exercised over those charged with the handling of money or stores.
- (3) To enable the members of the Local Authority to exercise due supervision over the employees.
- (4) To enable the Local Government Board to exercise due supervision over the Local Authority.
- (5) To enable ratepayers to judge as to the efficiency and economy with which the Local Authority discharges its duties.
- (6) To enable investors who have lent money to Local Authorities, whether upon mortgage or stock, to judge as to the soundness of their investment.

2.—Business men will be unanimous that Local Authorities should publish an Account of Income and Expenditure, and not merely an account of Receipts and Payments, and that being so, it is thought unnecessary to recite arguments in favour of this proposition. There is, however, something to be said in favour of a Receipts and Payments Account being also issued, although it seems doubtful whether the uses to which such an account can be put would justify the additional trouble involved. The actual accounts, however—that is to say, the books—should undoubtedly be kept upon a Revenue basis, and not upon a Cash basis, as with the last named it is

practically impossible to ensure that all moneys receivable are actually collected and brought into account.

3.—From the point of view of both ratepayers and investors one of the most important accounts would be one containing, in tabular form, the estimated expenditure under each heading, the estimated amount of spontaneous income available to meet such expenditure, and the balance proposed to be raised by rate. These figures should be contrasted with the amount of spontaneous income actually realised, the amount of rate actually realised, and the amount of expenditure actually incurred; thus showing the amount of the discrepancy between the estimate and the result, distinguishing between the discrepancy due to alterations in expenditure and that due to differences between the estimated and the actual income.

4.—For all the purposes enumerated above the periodical preparation of an adequate Balance Sheet is a *sine qua non*. In the case of all save the smallest Local Authorities there should be a separate Balance Sheet in respect of each Department, and an aggregate Balance Sheet, in tabular form, showing the combined position of affairs. These Balance Sheets should include all Capital Expenditure, but as further borrowings are sanctioned to pay for renewals of existing assets the original Capital Expenditure should be written off, so that from time to time the total appearing under each heading may represent, as nearly as possible, the cost price of actually *existing* assets. Such assets should be divided under the following headings:—

- (a) Unremunerative and unrealisable.
- (b) Unremunerative but realisable.
- (c) Remunerative.
- (d) Floating.

5.—Care should be taken to see that all Balance Sheets represent a complete statement of assets and liabilities up to the date thereof, and in particular accruing assets and liabilities should be brought into account, even although not received

or paid, as the case may be. In several cases Balance Sheets have been published misstating the position of affairs by omitting outstanding liabilities of considerable amount, and *per contra* in other cases assets have been omitted.

6.—It is suggested that the accounts might be materially simplified if it were found possible to so modify matters as to enable one rate to be levied by a Local Authority to cover all classes of expenditure incurred by it. The distinction at present observed between Borough Fund and General District Fund (or its equivalent) is extremely confusing to the uninformed, and appears to rest upon no recognisable basis, in that expenditure which with certain Authorities is charged against the one fund is with other Local Authorities charged against the other. I am aware that the rates for the two purposes are levied upon somewhat different principles, but it is clear that if the distinction between the two funds is not in all cases the same there can be no very recognisable principle underlying the distinction, which accordingly appears to be productive of complication without any compensating advantage.

7.—The question of Depreciation in connection with the assets of Local Authorities is one of paramount importance, and one which of late years has been productive of most of the hostile criticism against Local Authorities' accounts. The Departmental Committee has, I understand, no power to deal with questions of policy, but it is submitted that it is a question, properly arising out of the consideration of the form of accounts, that those accounts should show exactly what is being done, and (so far as may be possible) the true position of affairs. If, when application was made for borrowing powers, a Local Authority was required to obtain a separate sanction in respect of each separate item of expenditure, and the loan period of each sanction was fixed according to the estimated life of the asset to be acquired, as nearly as the same could be determined, then the statutory Sinking Fund instalments would correspond exactly with the proper Depreciation

charge; and thus the Revenue Account of trading departments, if charged with such Sinking Fund instalments, would show the true profit on such trading. Owing, however, to the system of granting loans for an equated period, there is, in point of fact, no such correspondence between the loan period and the life of each separate asset, and in many cases it cannot even be said that the loan period represents the average life of the assets proposed to be acquired. Where the loan period is shorter than the life of the asset, the charging of Sinking Fund instalments against Revenue has the effect of understating the true profits; where, on the other hand, the loan period is longer than the estimated life of the asset, the converse position obtains. It is impossible for anyone looking at the published accounts of a Local Authority to form any reliable idea of the true position of affairs, because the necessary information is not available. I suggest, therefore, that appended to all such statements of account should be a Table showing the estimated life of all the various assets acquired, under suitable headings; the amount of the Sinking Fund necessary to provide for the writing off of such assets out of Revenue during the estimated life; the amount of the Sinking Fund required by statute to provide for the extinction of the loan by the date of its maturity; and, in separate columns, the excess (or deficiency) of the statutory Sinking Fund, as the case may be. In order to arrive at the true profits of the undertaking the difference between these two last columns only need be taken into account; but in order to effectively provide for the renewal of assets as they wear out it is necessary that Revenue should be charged, in addition to the statutory Sinking Fund, with the *gross* amount of the deficiency thereof in respect of assets whose estimated life is less than their respective loan periods, as otherwise there will be no funds available to provide for the renewal of these assets when required, pending the time when—the corresponding loan having been redeemed—it becomes again possible to borrow the expenditure incurred in such renewal. I have recently had occasion to go at great length into this question in connection

with the accounts of the Electricity Department of the city of Bristol, and I think it might materially assist the Departmental Committee if the result of my inquiries could be placed at their disposal.

8.—It will be observed that I have not commented upon the existing forms of return prescribed by the Local Government Board. My reason is that these forms are so inadequate that I think it would be far better to approach the subject *de novo*, rather than from the point of view of considering what, if any, alterations should be made in these forms with a view to making them more effective.

9.—In conclusion, I should like to point out very strongly that in the nature of things no form of accounts, however admirably designed, can serve any useful purpose whatever unless steps be taken to enforce a strict responsibility for accuracy on the part of those responsible for their issue. To mention no other instances, the cases of the Shoreditch Borough Council and the Cardiff Corporation will probably be fresh in the minds of the Committee, and show that at least some members of Local Authorities and their employees do not seriously consider the importance of the published accounts being in accordance with the known facts. There seems to me no reason whatever why members of the Finance Committee of a Local Authority should not be held as strictly to account as members of the board of a joint-stock company, nor any reason why the officers of a Local Authority should not be held as responsible as the officers of such a company. So long as the present system of immunity exists it would seem waste of time to prescribe modifications in the existing form of accounts, for, after all, the question of form is of minor importance as compared with the substance.

MUNICIPAL TRADING DEPARTMENTS.—The audit of Municipal Trading Departments is a subject which has, since the publication of the last edition of this work, attracted no small measure of public attention and of public

criticism. That municipal enterprise should be viewed with suspicion—or even hostility—in many quarters is by no means surprising when it is borne in mind that these trading departments represent either (1) monopolies which might otherwise have been undertaken by private persons, presumably at a satisfactory profit, or else (2) an active competition with the ratepayers themselves, who are thus called upon in a measure to subsidise their rivals in trade. It is, however, only in so far as the audit of these accounts is concerned that it is necessary to consider the subject here.

From the point of view of the conscientious Auditor, the chief thing that calls for consideration is that the published accounts purporting to show the results of the trading should be *true* accounts, actually showing those results, and not merely accounts which, while perhaps satisfying the limited requirements of the Local Government Board, may be insufficient to enable the true position of affairs to be discovered, or perhaps even entirely misrepresent that position. Although the point is by no means universally conceded, it is thought that the *personnel* of the proprietorship can have no material bearing on the form that the accounts should take, and that therefore the ordinary principles of accounting should in all cases prevail. If this be admitted, the accounts of a municipally-owned water-works, electric-lighting works, gas-works, tramway, or any other public undertaking, should be framed upon the lines upon which it is usual to frame the accounts of similar concerns owned by proprietary companies.

If the accounts are to serve *any* useful purpose, they should be so framed that it may be possible to compare them with the results achieved by proprietary undertakings carried on in a similar business; and this, of course, is only possible if the apportionment of expenditure as between Capital and Revenue be made upon the ordinarily accepted lines.

At the present time, however, this is impossible, because in the accounts of Local Authorities the question as to what

expenditure is capable of being recorded as Capital Expenditure has in practice to be determined, not by the facts of the case, but by the willingness, or disinclination, of the Local Government Board to allow the expenditure to be defrayed by the issue of a Loan, and the Board's rules do not appear to be based upon any accepted principles of accountancy. Thus, one general rule is that no loans shall be sanctioned to cover the expenditure of wages paid to permanent employees, even although those employees may have been continuously engaged for weeks (or months) on end upon *bonâ fide* capital extension, while *per contra* the Board will occasionally allow an appeal *ad misericordiam*, and sanction a loan for purely revenue purposes. In one case at least, where a loan had been originally sanctioned, and the proceeds of that loan improperly applied for purposes other than those sanctioned, a second loan was permitted, upon terms; that is to say, Capital Expenditure was allowed to be debited *twice*, and Revenue benefited accordingly. These, however, are only a few of the difficulties that arise in practice, making any comparison between the accounts of trading departments of Local Authorities and the accounts of proprietary undertakings carrying on a similar business extremely difficult.

It is when the necessity arises for making a special provision for depreciation that a difficulty arises in this direction. With regard to gas-works and water-works, where—as has already been explained—the theoretical principles of the Double Account System prove sufficiently accurate for most practical purposes, there is no tendency towards any very marked difference of treatment, and municipalities are quite content to comply with their statutory requirements, and to provide by way of a Sinking Fund for the gradual redemption of Loans out of Revenue, while at the same time maintaining their Capital Expenditure intact (or approximately intact) by charging all repairs and renewals against profits. The result is that these undertakings, which were originally purchased by the Local Authority with borrowed money, are being gradually

paid for by the Local Authorities out of profits; and only the excess profits, after so providing for the gradual payment for the undertaking, are applied towards the relief of rates. With reasonably competent management no difficulty whatever ought to be experienced in arriving at this result, and yet applying annually a reasonable surplus of trading profits towards the relief of rates.

In some cases, however, the management has been defective, and in other cases the success of the undertaking has been handicapped from the outset by an unduly inflated Capital Account, which — combined with the lack of competent technical advice, and a desire to prove by results that the original enterprise was really justified — have produced a singularly unfortunate position of affairs in connection with the more speculative enterprises of tramways and electric-lighting. Here, as has been already stated, no true profit can be arrived at — at all events during the earlier years of an undertaking's existence — by the strict application of the Double Account System. In addition to charging actual outlay in respect of repairs and renewals against Revenue, a provision — and a fairly substantial provision — for Depreciation is essential if the true results are to be shown. These facts have been overlooked — it was thought, in the first place, inadvertently — and, now that their oversight has been challenged, attempts have been made to justify it that are hardly likely to meet with the acceptance of those who are competent to express an opinion upon the subject.

It has been argued that, inasmuch as there is no statutory provision *requiring* Local Authorities to provide for Depreciation, it is unnecessary for them to make any such provision; and it has further been argued that the provision of the statutory Sinking Fund takes the place of — and is in substitution of — Depreciation.

With regard to the first point, it has been aptly pointed out by the late Mr. EDWIN GUTHRIE, F.C.A., that no statute is neces-

sary to supplement the Common Law provision that accounts (of whatever kind) should be true accounts. If, therefore, provision for Depreciation be necessary to enable the accounts to show correctly the position of affairs, it becomes equally necessary from a legal point of view. It may, however, further be pointed out, in the first place, that the statute law *does* require the Capital assets of these undertakings to be "maintained" out of Revenue, and, further, that no profits are legally available to be applied towards the relief of rates until after such maintenance *and* Sinking Fund have been provided for. If the term "maintenance" be employed in its ordinarily accepted sense, a due provision for maintenance would cover not merely actual current payments, but also all necessary provision for payments which at some future time will be necessary to make good deterioration in value actually accrued to date.

With regard to the second point, as to whether provision for Depreciation and provision for Sinking Fund are interchangeable terms, it must, of course, be clear to those who duly appreciate the object of each that the two are by no means identical. It might, of course, be argued that, so long as the assets are really maintained intact out of Revenue, there is no urgent need to provide for the eventual repayment of loans. From the accounting point of view no such need, of course, exists; but from the legal point of view it is necessary, if for no better reason than because it has been decreed that permanent indebtedness is not to be allowed. That, however, is clearly not the way in which the subject was approached by the Legislature. The Legislature (there can be but little doubt) altogether overlooked the question of Depreciation, as such, deeming the statutory requirement that the assets should be "maintained" out of Revenue sufficient; but, for all that, it required the loans to be eventually redeemed, and—perhaps appreciating that "maintenance" (taking a narrow view of the term) would not involve any provision for obsolescence—it seems to have attempted, although quite roughly and often

quite unsuccessfully, to limit the term of each loan approximately to the life of the assets about to be acquired.

It is well to bear in mind, however, that although this rule has been invariably acted upon with regard to the more stable enterprises, the essentially speculative element in connection with all electrical work has been quite overlooked, with the result that many loans have been sanctioned, for electrical purposes, for periods far exceeding any reasonable estimate of the life of the assets. This fact has been admitted by the more enlightened Local Authorities, for all such duly appreciate the necessity for an adequate provision for Depreciation; but some (as, for example, Bolton) have claimed that, *if* due provision be made for Depreciation, it is unnecessary for provision to be made for Sinking Fund as well.

It is clear that, if no such separate provision be made for Sinking Fund, loans can only be repaid as they mature out of the assets which have been accumulated for the purpose of replacing Capital Expenditure as it becomes worn out. When, therefore, the necessity arises for undertaking extensive renewals, further borrowings will be necessary—a circumstance which, it is thought, is sufficient to demonstrate the non-existence of the statutory Sinking Fund in the meantime.

The policy of the Local Government Board—if, indeed, its somewhat conflicting regulations can be said to be governed by any policy whatsoever—would appear to be limited to an attempt to prevent money being borrowed for renewal purposes until the repayment of the original Loan has been provided for out of Revenue. In practice, however, this system will be found to result in extremely unequal charges to Revenue unless some serious attempt be made to equalise those charges by the provision of a Reserve for Renewals, or other form of Depreciation Fund. Theoretically, Loans are sanctioned for a term corresponding to the average life of the assets to be acquired therewith. Apart from the fact that the average life cannot be computed in advance, it is clear that—being an

average figure—it does not correspond with the life of each separate item, with the result that a considerable number of assets will in all cases call for renewal before the repayment of the original Loan has been provided for by the statutory Sinking Fund instalments. Whatever deficiency there may be under this heading at the date of renewal must then be provided for out of current Revenue, unless some provision has been made in advance against the Revenue of previous years. Thus, in practice, in all cases substantial payments for renewal purposes will have to be charged against Revenue; and, that being so, the charge ought in all fairness to be equalised as far as possible over a series of years.

The question has been raised as to whether it is competent for a Local Authority to provide a Reserve for Renewals or Depreciation Fund. The point is not altogether free from doubt, but in practically all cases there exists power to create a so-called “Reserve Fund” up to 10% on the capital outlay for the time being. Such a “Reserve Fund” would probably be sufficient to equalise expenditure upon renewals necessarily chargeable against Revenue; but, instead of being regarded as an optional allocation of profits, it should be considered as a necessary charge *against* Revenue prior to the ascertainment of true profits. The name “Reserve Fund” is thus clearly misleading.

In this connection it is of interest to note that the Institute of Municipal Treasurers and Accountants, in consultation with the Municipal Electrical Association, has passed the following resolutions:—

“That in the opinion of the Association, electricity supply undertakings having to be maintained in a thorough state of efficiency out of Revenue, no Depreciation or further writing off of capital is necessary when the period allowed for the repayment of Loans is not greater than 30 years, as the equated life of the works exceeds this period.”

“ That with regard to the formation of a Reserve Fund, this Association is strongly of opinion that such should be formed up to the limit allowed by the Provisional Order before any contribution is made in relief of the rates.”

These resolutions confirm the view already expressed, although they do not appear to sufficiently explain the circumstances under which the necessity arises for the early provision of an adequate Reserve for the equalisation of expenditure upon renewals.

It is impossible to deal adequately with this interesting subject within the limits of the present volume ; but it may be pointed out in conclusion that, if it be granted that adequate provision for Depreciation must in all cases be made, the additional sum required to provide for Sinking Fund as well would not, under normal circumstances, exceed (say) 1 per cent. on the Capital outlay. If, therefore, the trading undertaking be reasonably successful, these Sinking Fund instalments might well be provided for out of profits, while yet leaving a reasonable margin for the immediate relief of rates ; whereas, unless both Sinking Fund and Depreciation be provided for, the time can *never* arrive when the undertaking is free from debt.

The audit of municipal trading departments was very fully considered before a Joint Committee of both Houses of Parliament in 1903, and the Report of that Committee, which raises many questions of interest, is therefore reproduced in full as an appropriate conclusion to this section :—

“ The Select Committee appointed to join with a Committee of the House of Lords to consider and report as to the principles which should govern powers given by Bills and Provisional Orders to municipal and other local authorities for industrial enterprise within or without the area of their jurisdiction, have considered the matters to them referred, and have agreed to the following Report :—

“ 1. The present Committee may be regarded as continuing the inquiry held by the Joint Committee on Municipal Trading appointed in 1900, an identical reference having been made in each case.

"2. The evidence taken by the former Committee was of a general character, beginning with a detailed examination of the limits and restrictions now imposed upon the undertakings of local authorities by different Departments of State, by the authorities of both Houses entrusted with the regulation of private business, and by the practice of Select Committees. The former Committee then proceeded to some consideration of the general arguments advanced by advocates and opponents of municipal trading.

"3. In consequence, however, of the great extent of ground to be covered, and the complexity of the subject, that Committee were unable to make any report on the merits, but confined themselves to a recommendation of re-appointment in the next session.

"4. The present Committee, in view of the fact that they were not appointed until after Whitsuntide, and were unable to hold their first meeting before the 15th June, decided to take a different course.

"5. The Committee felt that any attempt to survey the general subject of Municipal Trading could only have led to a second postponement of the enquiry, as it would have been impossible for them in the short time available before the close of the session (when the existence of every Committee is terminated) to issue a report upon the whole subject.

"They agreed, therefore, to devote their attention to one or more distinct aspects of the question, passing by others until Parliament should be pleased to direct further enquiry.

"6. The first branch of the subject with which the Committee decided to deal was that of Municipal Accounts, with regard both to the form in which they are prepared, the systems under which they are audited, and the right of access to them possessed by the ratepayers. The evidence taken has been mainly directed to these questions.

"7. Whatever view may be taken of the proper limits, if any, which can be set to municipal trading, it is clearly important that, wherever it exists, ratepayers should be not less fully and continuously informed of the success or failure of each undertaking than if they were shareholders in an ordinary trading company.

"8. In a large number of cases this is undoubtedly done. But there is in some instances evidence to a contrary effect, and in view of the ever-increasing number and magnitude of municipal undertakings, it is most desirable that a high and uniform standard of account-keeping should prevail throughout the country.

"9. The Committee are doubtful whether it would be possible to prescribe a standard form of keeping accounts for all municipal or other local authorities, having regard to the varying conditions existing in

different districts. But they recommend that the Local Government Departments should invite the Institute of Chartered Accountants, the Incorporated Society of Accountants and Auditors, and the Institute of Municipal Treasurers and Accountants of England and Wales, and the Society of Accountants in Edinburgh, and the Scottish Institute of Accountants in Glasgow, to report and confer upon the matter.

"10. The Committee have directed full attention to the question of Audit.

"11. The Committee recommend that a uniform system of audit should be applied to all the major local authorities—viz., the Councils of Counties, Cities, Towns, Burghs, and of Urban Districts.

"12. At present Municipal Corporations in England and Wales, with a few exceptions, are only subject as regards audit to the provisions of the Municipal Corporations Act 1882, by which one Auditor, who must be a member of the Town Council, is nominated by the Mayor, and two, who cannot be members of the Town Council, are elected by the ratepayers.

"13. The evidence shows that no effective system of audit is thus supplied. The Elective Auditors are poorly paid, or are unpaid altogether, little interest is taken in their election, and although in some cases they are able to lay a finger on a particular irregularity, it is not clear that they could not make the same discovery in the capacity of active ratepayers. No complete or continuous audit is ever attempted by them.

"14. All County Councils, the London Borough Councils, and Urban District Councils are subject to the Local Government Board audit. This audit is carried out by District Auditors who, as a rule, are not accountants, and are not, in the opinion of the Committee, properly qualified to discharge the duties which should devolve upon them. By special local Acts the Corporations of Tunbridge Wells, Bournemouth, and Southend-on-Sea must, and the Corporation of Folkestone may, adopt the Local Government Board system of audit. The duties of the Auditors seem to be practically confined to certification of figures, and to the noting of illegal items of expenditure.

"15. To apply this system of audit to Municipal Corporations would arouse strenuous opposition from them, and the course may be considered impracticable; but in addition to this the fact that District Auditors are not accountants seems to unfit them as a class for the continuous and complicated task of auditing the accounts of what are really great commercial businesses.

" 16. The Committee accordingly recommend that—

"(a) The existing systems of audit applicable to Corporations, County Councils, and Urban District Councils in England and Wales, be abolished.

"(b) Auditors, being members of the Institute of Chartered Accountants or of the Incorporated Society of Accountants and Auditors, should be appointed by the three classes of local authorities just mentioned.

"(c) In every case the appointments should be subject to the approval of the Local Government Board, after hearing any objections made by ratepayers, and the Auditor, who should hold office for a term not exceeding five years, should be eligible for re-appointment and should not be dismissed by the local authority without the sanction of the Board.

"(d) In the event of any disagreement between the local authority and the Auditor as to his remuneration, the Local Government Board should have power to determine the matter.

"(e) The Scots practice of appointing Auditors from a distance, in preference to local men, to audit the accounts of small burghs should in similar cases be adopted in England.

" 17. The Committee are of opinion that it should be made clear by statute or regulation that the duties of those entrusted with the audit of local accounts are not confined to mere certification of figures. They therefore further recommend that—

"(a) The Auditor should have the right of access to all such papers, books, accounts, vouchers, sanctions for loans, and so forth, as are necessary for his examination and certificate.

"(b) He should be entitled to require from officers of the authority such information and explanation as may be necessary for the performance of his duties.

"(c) He should certify—

"(i.) that he has found the accounts in order, or otherwise, as the case may be ;

"(ii.) that separate accounts of all trading undertakings have been kept, and that every charge which each ought to bear has been duly debited ;

"(iii.) that in his opinion the accounts issued present a true and correct view of the transactions and results of trading (if any) for the period under investigation ;

"(iv.) that due provision has been made out of Revenue for the repayment of loans, that all items of receipts and expenditure and all known liabilities have been brought into account, and that the value of all assets has in all cases been fairly stated.

"18. Auditors should be required to express an opinion upon the necessity of Reserve Funds, of amounts set aside to meet depreciation and obsolescence of plant in addition to the statutory Sinking Funds and of the adequacy of such amounts.

"19 The Auditor should also be required to present a report to the local authority. Such report should include observations upon any matters as to which he has not been satisfied, or which in his judgment called for special notice, particularly with regard to the value of any assets taken into account.

"20 The local authority should forward to the Local Government Board both the detailed accounts and the report of the Auditor made upon them. It should be the duty of the Auditor to report independently to the Board any case in which an authority declines to carry out any recommendation made by him.

"21. A printed copy of the accounts, with the certificate and report of the Auditor thereon, should be supplied by the local authority to any ratepayer at a reasonable charge.

"22. After careful consideration the Committee are of opinion that in view of the thoroughness of the proposed audit, powers of surcharge and disallowance could be altogether dispensed with in the case of the major local authorities.

"23. Those powers could not, it is believed, be applied to Municipal Corporations in view of the strong objection expressed by them; and it is doubted whether their retention in the case of other authorities would compensate for the loss of uniformity which would result.

"24. The power of disallowance, applying as it does only to illegal expenditure, and not to unwise undertakings and enterprises, does not afford any real safeguard to the ratepayers whose interests are affected.

"25. With a continuous, vigilant, and thoroughly efficient system of inspection and audit, the surest guarantee to the ratepayers against extravagance is to be found in the deterrent effect of public exposure, in addition to the existing legal remedies.

"26. The dispensing power expressed by the Local Government Board under the Local Authorities (Expenses) Act 1887, throws on the department an amount of work often out of proportion to the importance of the issue involved.

"27. The Committee suggest that in view of the large changes recommended by them it might be advisable to create a new body, in the form of a Board of Commissioners of Local Audit, in some respects analogous to the Railway Commission. This body could be entrusted with the powers which the Committee recommend in their report should be vested in the Local Government Board.

"28. The Committee recommend that if in the case of Scotland it is thought desirable that the existing statutory audit of accounts of County and Borough Councils should be maintained, at any rate the system of audit for the five large cities, which is at present regulated by private Acts, should be assimilated to that which is recommended for the major local authorities in England.

"29. The Committee are of opinion that it would be advisable to continue investigations into other branches of the subject of Municipal Trading in a future session of Parliament."

No legislation has been attempted in consequence of the above recommendations, and indeed the late President of the Local Government Board stated, in the last Parliament, that it was not the intention of his Department to recommend any legislation as a result of this Report. Some twelve months' since the present President of the Local Government Board appointed a Departmental Committee to inquire and report as to the best methods of accounting for the use of Local Authorities, and the form that their published accounts should take. The Report of this Committee has, however, not yet been published.

So far as applicable, the method of audit described under the headings of the various industries concerned (*ante*) will be found useful in connection with the audit of municipal undertakings; but it is well to note, in passing, that Corporations are not bound to adopt the form of Gas Accounts set out in Schedule "B" of the Act of 1871. It would appear, however, that the form of Electric Light Accounts prescribed by the Board of Trade is applicable to such undertakings as may be in the hands of Local Authorities.

VII. EXECUTORS' AND TRUSTEES' ACCOUNTS.

—It will sometimes happen that the professional accountant is

called upon to audit the accounts of executors or trustees, on behalf of some dissatisfied beneficiary.

The purport of the Auditor's investigation in such cases will be to ascertain that the terms of the will or trust have been complied with, and that no improper use, or unauthorised investment, of the trust funds has occurred. Questions of apportionment between Capital and Income will also claim his attention.

The fullest investigation into details will be necessary, except perhaps where the trustees have been authorised to carry on the testator's business, and there is no suggestion that their conduct has, in this respect, been improper.

In addition to the will and probate, and the accounts kept by the executors and trustees, the Probate Account (with any subsequent corrective accounts)—or its more modern equivalent, the Account for Estate Duty—and Residuary Account, together with the Minute Book (if one be kept) and all documents and vouchers, will require to be carefully examined.

With regard to the question of apportionment, it is important to remember that all interest accrued to the date of death (inclusive) forms part of the *corpus*; that the profit or loss arising from any subsequent *bona fide* change of investment falls, as regards capital, upon capital, and as regards income, upon income; that, even where investments of a wasting nature are specially authorised, the whole of the income does not of necessity pass to the life-tenant—the usual custom being to consider four per cent. (or thereabouts) as income, and to capitalise the remainder (*vide Nicholson's case*, Ch. 1895); that any loss arising out of an unauthorised investment falls upon the trustees personally, who are liable to repay the amount with such interest as the Court may direct—the rate being usually four per cent. (simple interest), except where the trustees have applied the funds to their own use, when a higher rate is generally charged. Any of the above provisions may, how-

ever, be modified by the special terms of the will or other instrument creating the trust.

The investments authorised for trust funds (subject to any special terms in the will) have varied from time to time. The Auditor will therefore require to satisfy himself that each investment was a proper one *at the time it was made*. The following is a list of the chief investments authorised at the time of writing :—

Two and Three-quarters per Cent. Consolidated Stock (to be called after the 5th of April 1903 Two and a Half per Cent. Consolidated Stock) :

Consolidated Three Pounds per Cent. Annuities :

Reduced Three Pounds per Cent. Annuities :

Two Pounds Fifteen Shillings Annuities :

Two Pounds Ten Shillings per Cent. Annuities :

Exchequer Bills :

Bank Stock : (England or Ireland.)

India Three and a Half per Cent. Stock :

India Three per Cent. Stock :

Any securities the interest on which is guaranteed by Parliament :

Indian Railway Debenture Stock guaranteed by the Secretary of State :

Stocks of Colonial Governments guaranteed by the Imperial Government :

Mortgage of freehold and copyhold estates respectively in Great Britain or Ireland :

Metropolitan Consolidated Stock :

Debenture Stock created by the Receiver of the Metropolitan Police District :

Debenture, Preference, Guaranteed, or Rentcharge Stocks of Railways in Great Britain incorporated by special Act, or Ireland, having for ten years next before the date of investment paid a dividend on Ordinary Stock :

Nominal Debentures or Nominal Debenture Stock issued under the Local Loans Act 1875, provided in each case that such Stocks or Bonds shall not be liable to be redeemed within a period of fifteen years from the date of investment :

Local Loans Stock under the National Debt and Local Loans Act 1887.

As to powers of purchasing at a premium, see the Trustee Act 1893.

Under the Colonial Stock Act 1900, Section 2, the securities in which a trustee may invest under the powers of the Trustee Act 1893 shall include any Colonial Stock which is registered in the United Kingdom in accordance with the provisions of the Colonial Stock Acts 1877 and 1892, as amended by this Act, and with respect to which there have been observed such conditions (if any) as the Treasury may by order notified in the *London Gazette* prescribe.

It frequently happens that an estate is so bequeathed as to be dividable between persons of different ages, with the proviso that the share of each is to be held in trust for him until the happening of a certain event—such as his attaining his majority (or, in the case of a female, on her marriage)—the beneficiary in the meantime only receiving the income on his, or her, share. Under such circumstances it generally follows that the beneficiaries do not become simultaneously entitled to their respective shares in the principal: but the moment anyone becomes entitled to a share in possession he becomes entitled to actually receive his share, and—save by consent—the division (or partition) of the estate cannot be postponed. If the estate consists of investments that are readily capable of division, the problem is, of course, a quite simple one, for the beneficiary entitled to the partition may then have transferred to him (or sold for his benefit) his due fraction of each of the numerous investments held by the trustees; but when the estate includes mortgages, lands, or other non-divisible assets, some arbitrary method of arriving at the beneficiary's share becomes essential. If all beneficiaries are of age, the share of each may be mutually agreed: but if any one of the beneficiaries be under age, there is no means of obtaining his (or her) consent. The only course is then to apply to the Court, on an originating summons, when the Court will direct a "partition" of the estate, and the ascertainment of the share immediately payable to the beneficiary entitled to a possessory interest, and the order of the Court will be a protection to all.

parties concerned. Upon payment of the amount found to be due to the beneficiary, he ceases to have any interest in the trust estate, and the residue of the estate is then held in trust for the remainder of the beneficiaries, who alone are concerned in any subsequent fluctuation in the value of the trust investments.

It is especially important to remember that beneficiaries, unless of full age, have no power to consent to any variation in the terms of the trust.

In conclusion, it need hardly be pointed out that one of the most important duties in these audits consists of a very careful verification of the investments.

CHAPTER V.

SPECIAL CONSIDERATIONS IN DIFFERENT CLASSES OF AUDITS.

(Continued.)

VIII. ACCOUNTS OF INSTITUTIONS.—(a) CHARITIES.—Under this head may be included the accounts of Hospitals, certain endowed Schools and Almshouses, and similar institutions.

With regard to Endowed Charities, certain statutory provisions obtain ; but inasmuch as they do not practically affect the Auditor's position it has not been thought necessary to include them in the Appendix.

The distinguishing feature of most Charities' Accounts is the receipt of subscriptions and donations. These will, of course, require to be vouched in the usual way ; but, perhaps, the most effective check consists in the publication of a list of subscribers and donors along with the accounts.

In the early part of 1890 a Committee of the Charity Organisation Society appointed a sub-committee, consisting of four well-known Chartered Accountants, to inquire into the best methods of preparing and auditing the accounts of Charitable Institutions. This sub-committee devised *pro formâ* accounts, which were recommended for the use of various types of charitable institutions, and copies of these forms are reproduced below :—

FORM I.
SMALL CHARITABLE INSTITUTIONS WITHOUT PROPERTY OR TRADING OR INDEBTEDNESS AT THE
CLOSE OF THE PERIOD.

Dr.		A. B., Treasurer, in Account with "THE WEST HILL MISSION," for the Year ended December 31 1888.		Cr.	
<i>Receipts.</i>		<i>Payments.</i>			
£	s d	£	s d	£	s d
To Balance in Treasurer's hands, January 1 1888.	..	By Rent, Rates, Taxes, and Fire Insurance—			
" Subscriptions (as detailed) ..	£15 10 6	Rent ..	£40 0 0		
" Donations (as detailed) ..	79 8 4	Rates and Taxes ..	12 0 0		
" Money in Collecting Boxes ..	28 12 7	Fire Insurance ..	0 7 6		
" Weekly Offerings ..	20 11 4				
" Sale of Donations in kind ..	5 7 6	" Coals ..	52 7 6		
		" Gas ..	23 4 3		
Proceeds of Lectures, Concerts, &c.	45 11 6	" Repairs ..	12 5 0		
Less Expenses of ditto ..	34 19 6	" Provisions—	12 0 0		
		Tea ..	12 1 0		
		Milk ..	12 0 6		
		Bread ..	12 3 6		
		Butter ..	12 7 0		
		Sundries ..	12 6 5		
				60 18 5	
		" Entertainments—			
		Day in the Country ..	..	47 8 6	
		Printing and Stationery ..	..	8 5 6	
		" Postages ..	..	6 2 3	
					222 11 5
		" Cash Balances at December 31 1888—At			
		Bankers (naming Bankers) as per Pass			
		Book ..	£49 6 0		
		Less Outstanding Cheques..	16 6 0		
				33 0 0	
		In hand (Petty Cash) ..	4 11 11		
				37 11 11	
				£260 3 4	

We have examined the above Statement (Form I.) with the Books, Accounts, and Vouchers relating thereto, and certify the same to be correct.
We have verified the Cash Balances.

.....Auditors.

THE WEST HILL MISSION

SUBSCRIPTIONS AND DONATIONS received during the Year 1888.

Name.	Subscriptions.			Donations.		
	£	s	d	£	s	d
Anonymous—A. B., January 19 1888 .. ..	..	..	..	10	10	0
„ C. D., May 15 1888 .. ..	..	..	..	10	10	0
„ C. D., Nov. 1 1888 .. ..	..	..	..	5	5	0
„ A. B., December 25 1888 .. ..	..	0	10 6	5	5	0
Bates, Arthur	10	10	0	..	..	..
Charlton, William	2	2	0	2	2	0
Danbury, Edward	3	3	0	..	..	..
Milton, Thomas.. ..	15	15	0	..	..	..
Nelson Arthur (collected per) .. ..	..	..	..	4	6	4
Owen, Henry	15	15	0	..	..	..
Parker, Mrs.	10	10	0	..	..	..
Queen, Her Most Gracious Majesty The ..	21	0	0	21	0	0
Simson, Arthur	5	5	0	..	..	..
Taylor, Henry	10	10	0	10	10	0
Unwin, Mrs.	5	0	0	5	0	0
Valpy, Admiral Sir Thomas	10	10	0	..	..	..
Waverley, Henry.. ..	5	0	0	5	0	0
Carried to Treasurer's Cash Account ..	£115	10	6	£79	8	4

Note.—The above amounts represent actual Receipts during the year 1888. They do not include any Contributions or other Receipts outstanding at December 31 1888, even though such may have been received prior to the Audit and issue of the Accounts.

Auditor.

London, January 17 1889.

CHARITABLE INSTITUTIONS HAVING PROPERTY BUT NOT CARRYING ON TRADING OPERATIONS.

(A)—INSTITUTIONS WITHOUT CURRENT LIABILITIES AT THE CLOSE OF THE PERIOD.

Dr. A. B., Treasurer, in Account with the "DEAF AND DUMB INSTITUTION," for the Year ended December 31 1888. Cr.

Receipts.		£ s d		£ s d		Payments.		£ s d		£ s d	
To General Receipts—						By General Expenses—					
Subscriptions (as detailed)	.. ..	1,236	2 6			Salaries (give details) ..	.. ..	320	0 0		
Donations (as detailed) ..	.. ..	203	19 0			Wages (give sub-heads) ..	.. ..	195	11 2		
Legacies—						Provisions ..	.. ..	724	18 3		
Mrs. Jaue Davies ..	.. ..	£60	0 0			Wine, Spirits, and Beer ..	.. ..	63	1 1		
Sir Thomas Smithson ..	.. ..	50	0 0			Laundry ..	.. ..	21	19 3		
Lady Helen Wishart ..	.. ..	50	0 0			Coal, Coke, and Wood ..	.. ..	64	7 0		
(All free of Legacy Duty)						Gas ..	.. ..	25	18 3		
Payments on behalf of Children	.. ..	128	9 11			Medicine ..	.. ..	3	0 0		
Dividends and Interest—						Rent, Rates, Taxes, and Fire Insurance	.. ..	29	3 4		
Dividends on Investments ..	.. ..	91	12 11			(give details) ..	.. ..	32	3 5		
Interest on Deposits ..	.. ..	5	10 0			Repairs to Building ..	.. ..	24	6 5		
(Income Tax recovered on the above)						Travelling Expenses of Patients ..	.. ..	27	0 0		
Collections—						Clothing ..	.. ..			1,576	8 2
Offertories ..	.. ..	76	10 9			" Secretary's Office—					
In Almsboxes ..	.. ..	35	1 2			Salaries of Secretary and Clerk (give details)	.. ..	80	0 0		
Proceeds of Donations in kind..	.. ..	18	6 5			Stationery and Printing ..	.. ..	12	10 4		
Tickets for Annual Dinner ..	.. ..	43	6 6			Postages and Telegrams ..	.. ..	10	2 7		
Deduct Expenses of ditto ..	.. ..	45	19 0			Expenses of Special Appeal..	.. ..	10	12 1		
Deficiency carried per contra ..	.. ..	£2	12 6			Advertising ..	.. ..	9	11 2		
						Collector's Pouchage ..	.. ..	8	3 11		
						Petty Expenses ..	.. ..	5	9 9		
Note.—Amounts collected at the Festival						" Annual Dinner, Deficiency (See per contra) ..	.. ..	136	9 10		
Dinner amounting to £87 10s. 6d. are included in Subscriptions and Donations above.						" Balance carried down—Excess of Receipts over Payments for the Year ended December 31 1888 ..	.. ..	2	12 6		
								240	2 2		
						December 31 1888		£1,955	12 8		
To Balance of Cash at January 1 1888						" Investments—					
" Balance brought down, being excess of Receipts over Payments for the Year ended December 31 1888 (See Balance Sheet) ..	.. ..	445	8 9			Purchase of £300 3 per cent. Consols at 101½ per cent. ..	.. ..	305	12 6		
" Donations specifically appropriated (say for New Wing to Building) ..	.. ..	240	2 2			Deposit in Savings Bank ..	.. ..	150	0 0		
						Cash—				445	12 6
						Balances at December 31 1888 at Bankers (naming Bankers) ..	.. ..	2,225	13 5		
						In hand (Petty Cash) ..	.. ..	4	5 0		
								2,229	18 5		
								£2,685	10 11		

THE DEAF AND DUMB INSTITUTION.

SUBSCRIPTIONS AND DONATIONS received during the Year 1888.

Name.	Subscriptions.			Donations.		
	£	s	d	£	s	d
Anonymous—X., January 1 1888	105	0	0	105	0	0
„ W. V., June 24 1888 .. ..	..	..	..	52	10	0
„ X., September 29 1888 .. ..	..	..	..	21	0	0
„ G. L., December 31 1888 .. ..	..	..	..	10	10	0
Bowers, Henry	105	0	0	..	..	..
Broom, Stephen	105	0	0	..	..	..
Carter, Mrs.	52	10	0	..	..	..
Davis, Edward	10	10	0	5	5	0
Evans, Andrew	2	2	0	..	..	..
Fisher, Miss Jane	30	0	0	4	4	0
Grey, George	0	10	6	..	..	..
Hardy, William	10	10	0	..	..	..
Jones, Jonas .. .. .	..	..	..	5	5	0
King, William	10	10	0	..	..	..
Newman, George	1	1	0	..	..	..
Pope, William	2	2	0	..	..	..
Thompson, Arthur	3	3	0	..	..	..
Detail other Subscriptions, amounting to ..	798	4	0	0	5	0
Carried to Treasurer's Cash Account ..	£1,236	2	6	£203	19	0

Note.—The above amounts represent actual Receipts during the year 1888. They do not include any Contributions or other Receipts outstanding at December 31 1888, even though such may have been received prior to the Audit and issue of the Accounts.

Auditors.

London, January 17 1889.

AUDITING.

Expenditure.		£	s	d
To General Expenses—				
Provisions :				
Meat	£700 9 6			
Bread, Flour, &c.	790 15 0			
Milk	439 5 0			
&c. &c. (detail other accounts)	800 1 6			
Washing	2,730 11 0			
Fire, Lighting and Gas (give details)	114 2 0			
Rent, Rates, Taxes, and Fire Insurance (give details)	121 7 0			
Officers' Salaries (give details)	221 3 0			
Wages (give sub-heads and details)	602 5 0			
Medical and Surgical Expenses :	850 2 0			
Instruments and Repairs	430 2 2			
Drugs	650 0 1			
&c. &c. (detail other accounts)	820 2 1			
Funerals	1,900 4 5			
Hire of Ambulances	50 2 0			
Repairs and Renewals (give details)	20 1 6			
	200 0 0			
Secretary's Office—				
Salaries of Secretary and Clerks (give sub-heads)	300 0 0			
Stationery and Printing	36 3 6			
Postages and Telegrams	31 14 0			
Expenses of Special Appeal	37 10 0			
Advertising	32 2 6			
Collector's Pouchage	15 0 6			
Travelling Expenses	12 10 0			
Petty Expenses	5 1 6			
Depreciation Account—				
Amount written off cost of Fittings of the Hospital	100 2 6			
Balance, being excess of Income over Expenditure for the year ended December 31 1888, carried to Capital Account (See Balance Sheet)	130 0 1			
	£7,510 2 6			
Income.				
By Subscriptions—				
Annual (as detailed)	1,800 0 0			
Life (as detailed)	400 0 0			
Donations (as detailed)	2,200 0 0			
Dividends on Investments	2,100 0 0			
(Income Tax returned on the same)	600 0 0			
Rents of Real Property	400 0 0			
Collections after Sermons—				
St. Stephen's, Walbrook	73 2 6			
St. Mary's, Hornsey	70 1 0			
St. Michael's, Highgate	60 3 0			
St. John's, Upper Holloway	68 15 9			
St. George's, Hanover Square	68 5 3			
Grants from other Institutions or Funds—				
Sunday Hospital Fund	292 10 6			
Saturday Hospital Fund	207 9 6			
Cancer Hospital Trust	200 12 6			
St. Margaret's Nursing Fund	150 0 0			
Legacies—				
Miss Emma Burns	300 0 0			
Sir George Coran	250 0 0			
Lady Thurstead	200 0 0			
The Duchess of Winchester	150 0 0			
(All free of Legacy Duty)				
Collections in Almshouses	900 0 0			
Proceeds of Sundry Sales—				
Kitchen Stuff	23 2 6			
Rags and Waste Paper	22 17 0			
Patients' Payments	45 19 6			
	10 2 6			
	£7,510 2 6			

FORM II. (B)—*continued*.
THE GENERAL HOSPITAL.
BALANCE SHEET, December 31 1888.

Dr.

Cr.

	£	s	d		£	s	d		£	s	d
To Sundry Creditors—				By Cash—							
For Unpaid Accounts	239	17	6	At Bankers (naming Banker) on Current Account	170	2	7				
" Loan Account	1,200	0	0	At Bankers (naming Banker) on Deposit Account	200	0	0				
" Subscriptions—				In hand—Secretary's Imprest	20	0	0				
On Account of 1889, paid in advance ..	200	0	0								
				Sundry Debtors—							
" Capital Fund—				For Rents Outstanding .. .. .	..			390	2	7	
Amount at Credit, January 1 1888	34,695	12	6	" Invested Property (at cost)—	..			50	2	6	
Add (or Deduct a Deficiency)				Investments (giving details)	20,000	0	0				
Excess of Income over Expenditure for the				(State if held in trust, or, if incorporated,							
Year ended December 31 1888	130	0	1	in the name of the Society)							
				Real Property (giving details)	10,000	0	0				
				" Hospital Buildings and Land (state whether				30,000	0	0	
				Freehold or Leasehold) and Fittings as at							
				January 1 1888	6,100	2	6				
				Less Depreciation of Fittings, &c.	100	2	6				
				" Fire Insurance—				6,000	0	0	
				Five years (Balance paid in advance) ..	..			25	5	0	
								£36,465	10	1	

We have examined the above Statements, Form II. (B), with the Books, Accounts, and Vouchers relating thereto, and certify the same to be correct. We have verified the Cash Balances and the Investments.

.....Auditors.

.....18

THE GENERAL HOSPITAL.

SUBSCRIPTIONS AND DONATIONS received during the Year 1888.

Name.	Subscriptions.		Donations.
	Annual	Life.	
	£ s d	£ s d	£ s d
Anonymous—June 17 1888 ..	..	..	5 5 0
„ July 29 1888 ..	..	..	5 5 0
„ October 1 1888 ..	..	..	10 10 0
„ December 31 1888	21 0 0	..	21 0 0
Bishop, Henry .. ..	..	100 0 0	..
Bond, Mrs.	10 10 0	..	..
Cobb, Peter	5 5 0	..	..
Davenport, Andrew .. ..	..	100 0 0	..
Hall, Mrs.	5 5 0	..	..
Jenkins, John .. ..	..	200 0 0	..
Mann, Thomas	10 10 0	..	10 10 0
Moore, Henry	5 5 0	..	..
North, William	3 3 0	..	52 10 0
Palmer, Edwin	2 2 0	..	..
Rawson, Cecil	5 5 0	..	..
Thomas, Mrs.	5 5 0	..	..
Detail other Names and Amounts	1,726 10 0	..	1,995 0 0
Carried to Income and Ex- penditure Account ..	<u>£1,800 0 0</u>	<u>£400 0 0</u>	<u>£2,100 0 0</u>

Note.—The above amounts represent actual Receipts during the year 1888. They do not include any Contributions or other Receipts outstanding at December 31 1888, even though such may have been received prior to the Audit and issue of the Accounts.

Auditor.

London, January 17 1889.

FORM III.

CHARITABLE INSTITUTIONS HAVING PROPERTY AND CARRYING ON TRADING OR MANUFACTURING
OPERATIONS FOR THE PURPOSE OF EARNING MONEY OR SUPPLYING THE WANTS OF THE
INSTITUTION.

INSTITUTION FOR THE BLIND.

TRADING ACCOUNT for the Year ended December 31 1888.

Cr.

Dr.

	£	s	d	£	s	d		£	s	d		£	s	d
To Stock on Hand (Sundry Materials) January 1 1888 .. .. .	..	..	..	2143	3	1	By Sales of Goods Manufactured	6449	16	7				
" Goods and Materials Purchased .. .. .	..	..	..	4497	5	4	" Goods Manufactured Consumed by the Institution	100	0	0				
" Wages .. .. .	..	..	..				" Stock on Hand (Sundry Materials) December 31 1888	2103	0	5				
Mat Makers at own Home	11	6	9				" Balance, being the Loss for the Year ended December 31 1888, transferred to Income and Expenditure Account	359	18	8				
Brush Makers do.	63	14	5											
Basket Makers do.	212	14	0											
Brush Makers in Institution	410	10	3											
Basket Makers do.	183	4	1											
Chair Caners do.	82	12	4											
Firewood Makers do.	305	2	8											
Working Expenses—				1,269	4	6								
Carman and Boys' Wages	93	12	0											
Stable Expenses (including Rent, Rates, and Gas of Stable, and Keep of Horses)	217	12	1											
Tools	10	10	0											
Carriage of Goods	25	18	6											
Salaries—				347	12	7								
Teachers and Foremen	234	0	0											
Travellers	52	0	0											
Manager, Clerks, and Shopmen	279	13	6											
Commission to Travellers .. .. .	..	..	..	565	13	6								
Depreciation of Horses, Vans, and Stable Utensils .. .. .	..	..	..	139	10	8								
				20	0	0								
				£8,982	9	8								

FORM III.—*continued.*
INSTITUTION FOR THE BLIND.
BALANCE SHEET, December 31 1888.

Dr.

Cr.

	£	s	d		£	s	d
To Sundry Creditors—				By Cash in Hand—			
For Unpaid Accounts .. .. .	..	..	..	At Bankers (naming Banker) on Current			
Capital Fund—				Account	1,351	14	6
Amount at Credit, January 1 1888	18,930	18	1	At Bankers (naming Banker) on Deposit			
Add (or Deduct a Deficiency)				Account	400	0	0
Excess of Income over Expenditure for the				In Hands of Manager of Workshop	42	15	2
Year ended December 31 1888	836	3	7				1,791 9 8
				Investments—			
				£2,017 12s. 10d. 2½ per cent. Consols cost	2,024	11	0
				£10,130 8s. 4d. New 2½ per cents .. cost	9,987	6	6
				£60 Bank of England Stock cost	200	0	0
				£745 India 3 per cents cost	750	0	0
							12,961 17 6
				the Institution—Leasehold Buildings and Land			2,000 0 0
				" Sundry Debtors for Unpaid Accounts .. ..	..		1,350 7 8
				" Stock of Materials and Tools on hand.. ..	..		2,103 0 5
				" Horses, Vans, and Stable Utensils	201	0	0
				" Deduct Depreciation	20	0	0
							181 0 0
				" Furniture	320	0	0
				" Deduct Depreciation	30	0	0
							290 0 0
				" Collecting Boxes	85	0	0
				" Deduct Depreciation	4	0	0
							81 0 0
							£20,767 15 3

We have examined the above Statements (Form III.) with the Books, Accounts, and Vouchers relating thereto, and certify the same to be correct.

We have verified the Cash Balances and the Investments.

.....18

.....Auditors.

INSTITUTION FOR THE BLIND.

SUBSCRIPTIONS AND DONATIONS received during the Year 1888.

Name.	Subscriptions.						Donations		
	Annual			Life.					
	£	s	d	£	s	d	£	s	d
Anonymous—A. W., May 1 1888 ..	..	..	..	..	..	..	10	10	0
„ X. Y. Z., June 1 1888	10	0	0	..	..	..	10	10	0
„ A. W., November 1 1888	..	..	..	..	..	..	10	10	0
„ X. Y. Z., December 1 1888	10	10	0	..	..	..	10	10	0
„ X. Y. Z., December 31 1888	10	10	0	..	..	..	10	10	0
Archer, Miss Emily .. .. .	..	..	..	80	0	0	..	..	..
Bordwick, Andrew	52	10	0	..	..	..	..	..	..
Chartrey, Charles .. .. .	..	..	..	..	..	..	21	0	0
Dantry, Evan	10	10	0	..	..	..	..	..	..
Ellis, Mrs.	15	15	0	..	..	..	..	..	..
Fox, Arthur .. .. .	..	..	..	..	..	..	21	0	0
Lawson, George	2	2	0	..	..	..	..	..	..
Mason, Henry .. .. .	..	..	..	..	..	..	5	0	0
Norman, Percy	1	1	0	..	..	..	..	..	..
Oldfield, John	3	3	0	..	..	..	..	..	..
Perry, Sir James	1	1	0	..	..	..	..	..	..
Turner, Samuel	3	3	0	..	..	..	..	..	..
Detail other Names and Amounts ..	273	1	0	..	..	..	2	2	9
Carried to Income and Expenditure Account	£393	16	0	£80	0	0	£101	12	9

Note.—The above amounts represent actual Receipts during the year 1888. They do not include any Contributions or other Receipts outstanding at December 31 1888, even though such may have been received prior to the Audit and issue of the Accounts.

Auditors.

London, *January* 17 1889

An important matter—from the Auditor's point of view—is that charities are not liable for income-tax; it should, therefore, be seen that none has been paid, and that the tax deducted from dividends received upon investments has been refunded.

The following extracts from the "Instructions for the guidance of Secretaries," prepared by the before-mentioned sub-committee, will form an appropriate conclusion to this section:—

"1.—Where Form I. is used, the Cash Book should be kept upon a columnar method, so that the analysis appearing in the Treasurer's Cash Statement may be easily followed by the Auditors.

"2.—Where a Banking Account is kept, all cash balances should be paid into the Bank on the last day of the period to be reviewed.

"3.—A list of all books kept by the Institution should be handed to the Auditors, all the books being open to inspection.

"4.—In Forms II. and III. the accounts should be kept in a Ledger, opening in the form in which they will be presented in various financial statements.

"5.—(Immaterial.)

"6.—The books should be balanced and the Statements for audit prepared prior to the visit of the Auditors.

"7.—All Deeds and other Securities should be kept in a Deed Box at the Institution's Bankers, the box having three locks, the keys of which should be held respectively by the Treasurer, Secretary, and another member of the governing body.

"8.—(Immaterial.)

"9.—Before going to press the printer's proof of the Subscription Lists and Accounts should be examined by the Auditors.

"10. (Immaterial.)

“ 11.—All vouchers of payment should be arranged in the order of the dates of payment prior to the audit.

“ 12.—All Bankers' Pass Books, made up to the end of the period under review, should be at hand at the time of audit.”

Many of these points do not relate solely to Charities' Accounts, but will be found useful at all times ; they are, however, mentioned in this connection because they appear to indicate the lines upon which the audit should run.

(b) CHURCHES.—In many respects the audit of Church Accounts is a peculiarly thankless task. Apart from the fact that they are hardly ever submitted to the Auditor in anything approaching proper form, it is almost invariably the case that no effective internal supervision is exercised, and frequently large sums will pass through, say, a verger's hands without any proper check being kept upon his dealings.

The Auditor must check everything he can, and try to teach his clients the elements of commercial caution ; but it is probable that he will never feel *quite* happy with a church audit. The writer well remembers, upon one occasion, being refused permission to count a balance of over £100 (practically a running balance) that was in the hands of the verger : not long afterwards—but, nevertheless, after repeated warnings—the suspicions of the vicar were at length aroused, and the verger was instructed to pay his balance into the bank. It seems unnecessary to add that he was unable to do so.

(c) COLLEGES AND SCHOOLS.—These accounts call for but little comment. The usual method of audit may be said to consist of a “cross” between that employed in “Charities” and “Hotels” (*q.v.*), but it may be added that only a detailed audit is likely to be found entirely satisfactory.

Many UNIVERSITY COLLEGES are subject to the Statutes made by the Commissioners appointed under the Universities Act 1877, under which duly audited accounts have to be

submitted to the University. In most cases a tax is payable upon the amount of income received.

ENDOWED SCHOOLS are nominally under the control of the Charity Commissioners, to whom copies of the Annual Accounts should be forwarded. The principal point to be remembered is that the Governors have no power to apply the *corpus* of the endowment to current purposes.

IX. BUILDING AND FRIENDLY SOCIETIES, ETC.

—(a) BUILDING SOCIETIES.—The enormous number of frauds—some of them of disastrous proportions—that have occurred in the accounts of Building Societies should suffice to make the Auditor of these accounts more than usually cautious.

The Building Societies Act 1874 left the appointment of Auditors to be dealt with by each society in its rules, but it was generally considered that at least two Auditors must be appointed, the usual custom being for the directors to appoint one Auditor and the shareholders the other. In many cases, however, Chartered Accountants were not appointed, and it is probable that most of the disasters are attributable to this circumstance. This condition of affairs has been partially remedied by the Building Societies Act 1894, which requires that at least one of the Auditors shall publicly carry on business as an accountant. In the majority of cases the Auditors so appointed have been Chartered Accountants, but it will be seen that this is still not required by the statute; moreover, the wording of the section is so vague that cases still exist of accounts not being audited by *bonâ fide* public accountants at all. It is well, however, not to lay too much stress upon the evils attending the appointment of a wholly unqualified man as Auditor, for the danger does not by any means stop here. It will usually be found that the whole management of a building society virtually devolves upon one man, who—besides having both books and cash under his entire control—turns the whole of the board round his little finger. Add to this the

fact that many building societies are virtually banks (and this fact has not been materially altered by the 1894 Act), and that the system of bookkeeping employed is generally of the most primitive kind, and some idea of the responsibility of the Auditor's position may be gained. The complexion of affairs is hardly improved where there is more than one real worker upon the staff: any efficient system of internal check is all but unknown (except in a few—a very few—of the best and largest societies), while the class of man employed is usually very different, and very inferior, to the class of man employed in banks for work of a very similar nature.

The great majority of frauds that have been committed have remained undetected by reason of the very superficial examination bestowed upon the accounts by the Auditors; but cases have occurred in which the most detailed audit (conducted by unskilled men truly, but none the less detailed on that account) has failed to detect anything wrong.

The author's experience of Building Society Accounts—and these remarks apply equally to every class of accounts included under this heading—has convinced him of the extreme importance of checking every addition, posting, and voucher; of carefully verifying every amount received in redemption of mortgagees or paid out to investing shareholders; of comparing *every* Pass Book with the Ledgers, and both with the lists of balances; and of testing the latter at considerable length in respect of the calculation of interest. The income received from properties on hand must be verified in every possible way; and, where such income does not seem to be a fair return upon the book-value of the various properties, the latter should be either revised or supported by a Surveyor's valuation.

The deeds relating to all mortgages, and the securities relating to whatever other investments there may be, must also be examined by the Auditor, who will do well, in addition, to require the solicitor to certify that such deeds are all in order.

In the case of a building society of any pretensions the number of deeds that call for inspection will be very considerable, and accordingly a method of saving unnecessary labour will be found acceptable. In all well-managed concerns it will be found that the deeds relating to each separate mortgage are enclosed in a separate envelope, upon the outside of which is endorsed a *resumé* of its contents. If this endorsement has once been verified and the envelope has been sealed, it is thought that under normal circumstances no similarly detailed verification of the contents is necessary at subsequent audits. At each subsequent audit all fresh sets of deeds must, of course, be verified in detail, as must also the contents of those envelopes which for one reason or another have been opened during the current period, and upon which therefore the Auditor's seal is not intact; but it is thought that where the seal remains intact, and, where a sufficiently distinctive seal has been employed, any further detailed investigation is unnecessary. It should be sufficient for practical purposes to verify the contents of a few envelopes, taken at random, and also, of course, the contents of all envelopes which in the opinion of the Auditor may by any possibility have been tampered with.

It is more than probable that the fees attaching to his office will afford the Auditor no adequate remuneration for an examination conducted on such lines as those laid down; but, be this as it may, the Auditor who—under ordinary circumstances—omits any of the precautions named would be worse than foolish.

It must also be remembered that there is a statutory limit to the borrowing powers of a society, which must not be exceeded. Another point to be borne in mind is that the Balance Sheet and accounts are now required to be kept in such form as the Registrar of Friendly Societies may prescribe.

The statutory requirements concerning, and the prescribed form for, the Accounts of Building Societies will be found duly set forth in Appendix "A."

(b) FRIENDLY SOCIETIES.—The Friendly Societies Acts 1875 and 1896 contain certain provisions (for which see Appendix “A” hereto) which will guide the Auditor in his work; beyond these statutory requirements the general considerations discussed under the head of Building Societies will apply equally to the Accounts of Friendly Societies, except that the different nature of the business carried on will somewhat alter the scheme of audit and assimilate it more closely to that followed in the case of Insurance Companies.

Unless the Auditor be a “public” Auditor holding an appointment under the Treasury, the accounts must be certified by two Auditors; but two partners in the same firm will satisfy the requirements of the Act. It is, perhaps, worth while to remember that the actuary employed at the quinquennial valuation need not be a “public” valuer.

Friendly Societies are required to keep hung up in a conspicuous place a copy of their last Balance Sheet, and to present a copy of their accounts free of charge to any member who may demand it, while every member has a right to inspect the books of the society at all reasonable times.

(c) TRUSTEE SAVINGS BANKS.—In connection with the audit of these accounts the Savings Banks Acts 1863, 1891, and 1893 will require to be studied, and in Appendix “A” will be found such portions of these Acts as affect the Auditor in the discharge of his duties. The 1863 Act prescribes the form in which the annual return is to be made.

The remarks in connection with the Accounts of Building Societies will apply, so far as they are relevant, with equal force to the Accounts of Savings Banks. The examination of all the Pass Books is a most important feature, and it must not be forgotten that there is a statutory limit both to the amount standing to the credit of any one depositor, and to the amount that may be paid in by a depositor in any one year.

A general supervision of Savings Banks is vested in an Inspection Committee appointed under the Act of 1893. This Committee is required to report to Parliament annually, and the reports that have already been submitted will be found of considerable interest to the Auditor. The present Committee is one of considerable experience. In the report for the year 1893-94 it was stated—after citing the duties laid down in Section 6 (6) of the 1863 Act:—Under No. 1 of the above headings the books of the bank may be taken to comprise—

“(a) In all cases, Deposit Ledgers with one or more daily Cash Books, or other record of the individual cash transactions with depositors. These books, at least, must therefore necessarily be examined not less than once each half-year to comply with a minimum requirement of the Act of Parliament.

“(b) In certain cases, a General Ledger and General Cash Book, or cash summaries, in which the totals of the daily transactions are periodically worked up to show the aggregate sums deposited and repaid.

“From the reports received the examination of the detailed cash records (which 182 banks keep in duplicate) does not appear so thorough as might be desired, though doubtless there may be a considerable amount of examination not mentioned by the Auditors in their reports, nor referred to in the reports of the inspectors.

“This is especially noticeable in the checking of the daily additions of these books, or schedules, in the regular checking of the cash remittances to the treasurer by a reference to the Bank Pass Book, and of the cash balance by actual enumeration. Although there may be some details of examination which have not been defined in the Auditors’ reports, the statistics obtained do not convey any very great assurance that the scrutiny brought to bear upon the Cash Books by the Auditors in the majority of cases is a searching one, and it

would thus appear that in many instances the audit in this respect ought to be supplemented.

“The examination of the Deposit Ledgers, on the other hand, appears to be much more complete, notably the detailed postings from the Cash Book. The additions and subtractions in the Ledgers, it is true, come in for but a small share of attention; but the verification of Pass Books, so far as it extends, is a test of the accuracy of these operations, as well as, to some extent, of the postings. The calculation and addition of interest is decidedly a weak point in the management of banks where there is only one paid officer. Though checking these items can hardly, in ordinary circumstances, be held to be the function of an Auditor, still, the Auditor seems at times to be the only person available to test their accuracy. Unless the Auditor does it, no independent check is brought to bear upon the items of interest at banks where only one paid officer is employed, and errors in calculation are apt to remain undetected. Any such defect should be seen to, even if some additional expense is incurred thereby; the cost to be met, where necessary, by corresponding economies in other items of Management Expenses.

“The most marked feature of a Savings Bank Audit appears to be the examination of the lists of balances extracted from the Deposit Ledgers. Two hundred and twenty-five Auditors certify that they have checked this independently, and eleven that they have done so with the aid of some member of the staff of the bank, a test that is not usually sufficiently independent to be safely relied upon. The importance of this operation will be appreciated when it is remembered that in most banks the total of the list is the only independent evidence of the aggregate liability of the trustees to the depositors, and it is necessary, therefore, to enable the Auditor to give a true certificate as to the amount of liabilities and assets. It also furnishes a check upon the accuracy of the postings in the Deposit Ledgers in the aggregate. As a check upon fraud the list is of little worth, unless made accessible to depositors, and

even then, before it can be put to much use, it is necessary to give every publicity to the existence and purpose of this volume by means of proper notices. Little reliance ought, therefore, to be placed on this statutory check upon fraud.

“As a rule, ‘the books of the bank’ include a General Ledger and General Cash Book in the larger and better managed and audited banks only, but we suggest that such books should be adopted by all Savings Banks, large and small. These books, or corresponding summarised statements, should be made up not less frequently than once a month, and ought to be checked by the Auditor throughout in all respects as to additions, transfers, and postings, either continuously month by month (where a visit of such frequency is possible), or at other longer intervals.

“Other books of account relate to Stock business, in which there is but little scope for error of any serious moment.

“AUDITORS’ REPORTS.—Our experience during the past three years shows that a clear report in writing, not less frequently than once every half-year, has not always been given, a minority of banks being still content with an annual report only.

“LIST OF BALANCES.—As already stated, the examination of this list is usually well attended to.

“CERTIFICATE OF LIABILITIES AND ASSETS.—This requirement can now in all cases be conveniently complied with by the Auditor certifying the Annual General Statement of Account (which, as last amended, contains a form of Balance Sheet) as having been examined and found correct.

“BOOK OF BALANCES.—As mentioned already, this book should bear a clear certificate as to its accuracy. At nearly all Banks it is so, but some cases still occur where the accuracy of this book is either not certified by the Auditor, or is certified by implication only. A form of certificate suggested by Mr. BOOKER (one of the late temporary inspectors) was given on page 74 of our First Annual Report.

“EXAMINATION OF PASS BOOKS.—It appears from the reports rendered that 178 Auditors attended at the Savings Banks from time to time to examine the Pass Books. Twenty-eight (apart from Savings Banks in Ireland, where this is compulsory) attended at periods of audit only. These figures would seem to indicate that the Auditors dispense with this test in certain cases where the trustees and managers themselves compare the Pass Books with the corresponding accounts in the Ledgers.

“One-hundred and sixty-eight Auditors of Savings Banks, other than those in Ireland, gave the number of Pass Books examined, and from these it would appear that the percentage thus verified varies from 13 per cent. to 39 per cent. in the case of Banks with deposits over £100,000, the average being 18 per cent.; from 18 per cent. to 32 per cent. where the deposits do not exceed £100,000, but are over £40,000, average 29 per cent.; and from 20 per cent. to 31 per cent., average 28 per cent., where the deposits are under £40,000. At Irish Banks the average percentage is 57, and at Banks in the whole Kingdom in respect of which figures are obtainable the average percentage is 20.

“These figures give, without doubt, more favourable ratios than would be the case if the data were supplied in every instance. It may be safe to assume that figures are mostly given in the cases where the examination was made to an extent above the average. In several cases, too, the numbers stated to be examined include books left at the Savings Bank for audit, and in some (where the audit is not conducted at the Bank office) the Auditor states that he has examined such Pass Books as were sent to him by the actuary, practically a useless proceeding, unless coupled with extraordinary precautions. It may, therefore, be advisable to recall to mind the remarks on page 10 of our Second Annual Report to the effect that Pass Books should be compared as brought in by the customers, and not left for inspection for days and weeks at the Banks.

“OTHER DETAILS OF AUDIT.—Receipts are taken from depositors at 120 Banks out of 236 from whose Auditors reports were received, and have been checked at 28, and tested at 27. There is a general feeling amongst the Auditors that it is too much to expect them to verify signatures to any extent.

“Expenses of management have been sufficiently vouched in 193 cases.

“The double check upon cash transactions with depositors appears to be complete and to be completely recorded at 204 Banks out of the 236. Of these 204, 182 record the use of the double check in two independent Cash Books, while 22, having only one Cash Book, post the Ledgers at the time from the entries in the Pass Book, thus recording each transaction in two ways before the Pass Book leaves the Bank. This method, although it might serve to trace any discrepancy in balancing the cash, does not afford a check on the total of the cash transactions for the day. It is only in use as a rule, however in the smallest Banks: but, to make it more complete, the accounts operated upon might be marked by inserting tags or other markers in the Ledgers, and the postings should be checked with the Cash Book, and the Cash Book summed a second time before the business of the day is concluded. The removal of all the tags, or other markers, from the Ledgers would show when all the postings had been checked.

“The double check is wanting, or is insufficiently recorded, in 32 cases out of the 236.

“Valuable assistance in the work of audit is occasionally rendered by the trustees and managers, either acting individually or by forming themselves into small audit committees. In the former manner a trustee or manager, willing to personally undertake some detail of audit, could most usefully direct his attention to the examination of Pass Books with the Ledgers of the Bank. The work of an audit committee would more especially be valuable in connection with the examination of the Cash Book, and of monthly or other statements of business

done. This would be particularly the case at Banks where it is not usual for the Auditor to undertake more than a half-yearly or quarterly audit, apart from any continuous examination of Pass Books that he may be called upon to make.

"We deem it of essential importance that the rules of all Savings Banks should make provision for the following matters:—

- "(a) For the examination of Pass Books during the year as presented by depositors and their comparison with the Ledgers to the extent of 10 per cent. of those extant, either by the Auditor or by some other independent person or persons.
- "(b) For the examination by the Auditor of the annual general statement and its certification by him, if found correct. If he is not satisfied, the Auditor should report accordingly to the trustees and managers.
- "(c) For the Auditor to render occasionally, when desired, a list of work done by him in the course of his audit."

The above extracts are of value, as showing the usual practice in addition to that which experience has shown to be desirable.

(d) CO-OPERATIVE SOCIETIES, &c.—The consideration of the audit of these accounts need not be entered into fully. Certain statutory provisions (which will be found in Appendix "A") must be complied with; but, in other respects, the audit will follow much upon the same lines as that of ordinary trading concerns.

Like all classes of audit enumerated in this section, the audit of Co-operative Societies' Accounts—to be effective—must be detailed and should be continuous. It may be added that—at all events, so far as the smaller Societies are concerned—the small number of employees militates against an effective

system of internal check, which, combined with the small salaries usually paid, makes it important to take every precaution against fraud.

It is greatly to be regretted that the statutory provisions as to the audit of these accounts, and also those of Friendly Societies, tend to discourage the employment of qualified accountants as Auditors. The provision that one "Public Auditor," or two other Auditors, must certify the accounts would have been valuable, had proper precautions been taken to ensure that only properly qualified persons were appointed "Public" Auditors by the Treasury. Doubtless many Public Auditors are well qualified to discharge their duties; but as much certainly cannot be said for all, while the evil is further aggravated by the fact that further appointments are only made as vacancies occur, so that a sort of monopoly exists, backed up by a statutory authority, which certainly cannot be supported upon its merits.

The accounts of Co-operative Societies are made up to the 31st of December in each year, and a return in the prescribed form must be forwarded to the Chief Registrar of Friendly Societies before the 31st of March following.

X. PROFESSIONAL ACCOUNTS.—(a) SOLICITORS.

—It is not easy to effectively audit the accounts of solicitors without devoting considerably more time to the task than clients would be willing to pay for, and nothing short of a continuous audit appears to meet the necessities of the case.

When a system such as KAIN's System of Bookkeeping for Solicitors is employed, it would appear to be of especial importance that the Auditor should satisfy himself that every entry in the Cash Journal is duly recorded in the proper column, for its insertion in the wrong column may easily produce an entirely false result. For this reason it is thought that most Auditors will deprecate the employment of the system where the Cash Journal is kept by the cashier. These comments are made not with the express purpose of drawing

attention to the shortcomings of a system in very general use, but merely because the system is, on account of its convenience, so frequently employed that the present work would not be complete without this passing reference to the difficulty of auditing accounts so framed. In the author's opinion the system is unrivalled where the principal, or one of the partners, himself keeps the Cash Journal: but in the case of those medium-sized firms where the principals cannot give individual attention to the books, and where the connection is not sufficiently large to make it practicable for the account-keeping to be organised upon a regular system of internal check, there would appear to be grave difficulties of verification which more than compensate for any immediate convenience in record.

The amount included in the Balance Sheet for outstanding charges should, in general, be verified by comparison with the draft Bills of Costs. Agents' Accounts should at all times be carefully considered, and it is not a bad plan to compare every item of costs charged up with the press copy of the bill rendered, the object being to make sure that the full amount chargeable has been debited, for the amount asked for may not (by reason of an amount having been received on—or in—account) be always the amount that has to be debited.

Of recent years the increasing number of fraudulent failures on the part of solicitors has drawn attention to the importance of proper accounts being kept by those who wish to avoid any possible reflection upon their manner of dealing with the moneys entrusted to them by their clients. At more than one meeting of the Law Society attention has been drawn to the importance of clients' moneys being kept quite distinct from the moneys of the practitioner himself. It is impossible to overstate the importance of this distinction, while it may be added that in many respects it materially simplifies the keeping of the accounts. Each large estate should have its own separate Bank Account and separate books, entirely independent of the books of the firm, while all other moneys

received in trust for clients should be paid into a "Clients' Account," and a separate column provided in the Cash Book for keeping this account distinct from the "general" Bank Account. Not the least important advantage of keeping the accounts of large estates quite separate from the general accounts is that the cost of keeping them, and of having them audited, may then frequently be charged against the estate in addition to other costs. Moreover, these accounts can be submitted to the clients (or their agents) for audit without disclosing any other transaction; and if they be so audited at regular intervals it is frequently unnecessary for them to be also audited by the solicitors' Auditors, and by this means a further saving of expenses may be effected.

(b) STOCKBROKERS. — A considerable amount of mystery appears to envelop Stock Exchange Accounts, and the remark has frequently been made that the audit of Brokers' and Jobbers' Accounts is altogether too technical a matter to be safely conducted by the general practitioner. The advantage of special practical knowledge on the part of the Auditor has already been freely admitted by the author, but it is contended that the desirable knowledge may be readily obtained, even by the general practitioner; and, with Stock Exchange Accounts in particular, it is suggested that the necessity of "specialism" has been greatly exaggerated.

For the audit of these accounts to be of any value, however, it is necessary that it should be of the most detailed description: the danger of error or fraud—either of which might assume alarming proportions—is extremely great, and the utmost care and circumspection are, therefore, imperative. Particular attention should be directed to the Name Ledger, and *Continuations* must also be carefully traced. The question of "splits" should also be kept in mind, as—although not a large item—it is a likely source of petty fraud.

Perhaps the chief danger in this class of audits lies in the fact that in the great majority of offices there exists no regular

system affording a reliable internal check, and no efficient supervision. To remedy this obvious weakness the visits of the Auditor should be frequent, say, at least once during each account; indeed—although a “completed” audit is doubtless useful, as affording a reliable periodical statement of accounts—the only really efficient audit of Stock Exchange Accounts would appear to be one that is both detailed and continuous.

(c) ARCHITECTS.—The accounts of architects are, perhaps, less frequently the subject of professional audit than either of the two classes of accounts just discussed, but this is a state of affairs which is always undesirable, and particularly so in cases where two or more architects are practising in partnership.

The accounts do not, as a rule, involve a particularly voluminous record, and it is therefore desirable that in all cases the audit should be a detailed one. The fact that architects are frequently not business men makes it important that the Auditor should take every precaution to guard his client from loss, both through actual fraud and bad bookkeeping; it is therefore important for him to see that every item in the Cash Book is properly vouched, and, so far as possible, that all fees and commissions are duly accounted for. It may be mentioned here that, with regard to fees payable to an architect for supervising the erection of buildings, these fees are payable by way of a commission—generally at the uniform rate of 5 per cent.—upon the value of the work done, as certified by the architect for the purpose of assessing the payments to be made on account to the builder. There will always, at balancing time, be a considerable amount of accruing fees, which, although not actually due for payment at the time, constitutes an asset; a schedule of these items should be prepared and certified by the principals for inclusion in the accounts. Many practitioners, however, work their accounts exclusively upon a cash basis, and the plan has much to recommend it when professions are concerned.

Another point that must not be lost sight of is that, in all important undertakings, a "Clerk of the Works" is appointed to be on the spot, for the purpose of checking the material and workmanship employed by the builder. The Clerk of the Works is not infrequently appointed by the architect, but he is invariably paid by—and is the servant of—the architect's client; if, therefore, for reasons of convenience, his salary has been paid by the architect, it is important to see that it is subsequently recovered by him.

DISTRICT SURVEYORS.—Under the Metropolitan Building Acts "District Surveyors" are appointed to supervise the construction and alteration of all buildings within the Metropolitan area. These District Surveyors are invariably architects, although in the case of all recent appointments the London County Council has stipulated that those occupying the position should give up their general practice. A few of the appointments, however, still remain in the hands of practising architects. It is both desirable and convenient that, in these cases, the accounts of the District Surveyor should be kept quite separate from the general accounts; and, as certain returns have to be made to the London County Council from time to time, it is convenient that the books should lend themselves to the preparation of these returns with a minimum amount of trouble. As, moreover, the collection of fees will then almost invariably devolve upon an employee, it is desirable that every reasonable safeguard should be adopted with a view to prevent the possibility of fraud.

The best system to adopt is to employ a tabular Ledger, in the same form as that in which returns have to be made to the County Council, with additional money columns on the right-hand side for the purpose of recording the receipt of fees during the current and the following year. Should any fees be still outstanding at the end of the following year these may be transferred to another folio, but the probability is that they will be so few in number as to prevent the additional labour thus

involved being any serious objection. The fees actually received should be entered in the Collection Book, which is a Cash Book with no credit side to it; and it will probably be convenient to have a separate Cash Book, recording the manner in which these fees have to be accounted for to the cashier at the office—or, if thought better, a credit side could be added to the Collection Book for this purpose. In practice, however, the former method is more convenient, as the Cash Book can then be kept at the general office, and the Collection Book at the district office, where, of course, it will be continually in use.

(d) MEDICAL MEN.—There are so many different systems of bookkeeping employed by medical men that it is difficult to afford any useful hints as to the method of audit in the space here available. It may be pointed out, however, that it is not, as a rule, either necessary or expedient for the Auditor to go behind the debits in the Patients' Ledger, which, as often as not, are fixed at round sums by the practitioner without any strict reference to the number of visits. It is desirable, however, that the Auditor should see that some efficient system of recording visits is in force, so that his client has all the facts before him when assessing the amount of his charges. The Auditor should carefully check the credit side of the Patients' Ledger, noting in particular any allowances that have been made, and he should see that all cash credited to patients has been properly accounted for.

Where payments have been made on account of patients, whether for medicines, or for consultation fees, &c., it is very important that the Auditor should see that they are properly charged up and collected in due course. Many practitioners employ one or more assistants, or dispensers, who are authorised to receive money, and where this is the case it is especially important that the system in use should, as far as possible, follow the ordinary commercial precautions against fraud. With those practitioners who supply their patients with medicines it is also necessary that the accounts of druggists,

&c., should be carefully checked, and an allowance will have to be made at balancing time for the value of drugs in stock.

It need hardly be added that where horses and traps are the property of the practitioner, an adequate allowance must be made for depreciation, probably at the rate of 15 per cent. or 20 per cent. per annum. Where, however, these are "jobbed," it is equally important to see that the cost of hire to the date of balancing is included; or, if this has been paid in advance, that a proportionate part is held over as an asset.

In concluding this portion of the work, the author cannot but feel that in spite of the very considerable space that has been devoted to the consideration of the special features attaching to the audit of different classes of accounts, the subject has been only very imperfectly dealt with. When, however, it is remembered that an exhaustive treatise upon the audit of any one class of accounts might easily approach the dimensions of the whole of the present work, it is hoped that it will be conceded that—however desirable it might have been to have considered the various questions involved in further detail—more could not have been reasonably expected within the limits of this volume.

CHAPTER VI.

FROM TRIAL BALANCE TO BALANCE SHEET.

THAT which forms the most important part of every audit, the question of principle involved in the preparation and certification of the Balance Sheet and Trading and Profit and Loss Accounts from the Trial Balance, will now be considered. It is especially desirable that in every audit the principal should give these subjects his personal consideration, not merely because of their intrinsic importance, but also from questions of policy which have already been dwelt upon.

As the points now about to be discussed are the most important, so are they also the most debatable, accountants of the highest repute being by no means agreed as to several of the principles involved. On the other hand, it would seem to the acute observer that much of this apparent difference is, in reality, merely verbal, while perhaps more is due to the inherent difficulty that exists in casting abstract principles into a concrete form. It is, indeed, not unreasonable to suppose that, in any case stated, there would not exist among our leading practitioners any radical difference of opinion as to what the profit of a company had really been; the real cause of the confusion appearing to be that, while one maintains the true net profit to be deducible from the Profit and Loss Account, another maintains that the Balance Sheet is the only reliable basis. It would seem that, if both Balance Sheet and Profit and Loss Account be correct, it matters but little which is called the cause and which the effect.

Throughout the course of this chapter the endeavour will be to view the various questions of principle from the broadest possible standpoint. It is true that, by this means, the inherent difficulty of the considerations involved will not be escaped; but it is hoped that at least the treatment will be found free from catch-words and all other sources of superfluous mystification.

PRINCIPLE IN VALUATION OF ASSETS.—It being the primary object of most ordinary undertakings to continue to carry on operations, it is but fair that the assets enumerated in a Balance Sheet be valued with that end in view; before this subject is pursued any further, however, it is well to acknowledge the two *essentially different* features obtaining to different classes of accounts. Certain Parliamentary companies, constituted for the purpose of undertaking public works, are, on account of the peculiar circumstances under which they were called into existence, required to render their accounts in a special form, under what is called the **DOUBLE ACCOUNT SYSTEM**. It being required that all capital raised by these companies shall be expended in the construction of the public works (for which purpose they were called into existence), care is taken by the Legislature to see that this provision is duly complied with; hence a special form of account, in which all moneys received and expended in the construction of the works are separated from the General Balance Sheet. Now, in order that this account (the **Capital Account**) may perpetually show that—and how—the capital authorised to be raised (except a small margin for working capital or contingencies) has actually been spent only upon the authorised purposes, it is necessary that the actual amount expended on the works be debited to the account, regardless of any alterations in value that may afterwards occur. It would, of course, have been easy for the Legislature to have provided that any fluctuation that might occur should be duly allowed for in the General Balance Sheet; but, having regard to the fact that no such fluctuation

could in any way practically affect the company, so long as it carried on business, and bearing in mind also the fact that it was contemplated that the company should *permanently* carry on business, it would appear that all consideration of these fluctuations was considered superfluous. With an eye to the future, however, and doubtless also with a view to—so far as possible—ensuring the business being permanently carried on, it was provided that the company's works (which were required to be kept perpetually at the amount of their initial cost, regardless of their after value) be continuously kept in a state of efficiency, and that the cost thereof be borne out of Revenue.

It will thus be seen that the *form* of the Double Account System arose from the statutory requirement that all capital raised should be used for the carrying out of the works for the execution of which the company was created; and that the principle that, so long as the works were maintained in a state of efficiency, their actual value need not be periodically reconsidered, arose from the circumstance that it was contemplated that the work authorised would be permanently carried on. How far these considerations need affect one's judgment concerning the valuation of the assets of undertakings not specifically covered by the statute it will now be necessary to enquire.

Taking first the case of ^gprivate traders, whether *sole* or firms, it is not difficult to see that, inasmuch as no man can reasonably hope to live for ever, the business of such an one is ephemeral as compared with that of a Parliamentary company. It is true that the business may, and frequently does, live longer than its founder; but to do so involves a change of proprietorship, and with it a *re-valuation of assets*. It will thus be seen that, although there is no necessity to consider the contingency of liquidation (at what are expressly known as "knock-down" prices), not merely the contingency but also the eventual certainty of a re-valuation must be faced. The basis of such a valuation will be that known as "as a going concern," and

it will, perhaps, be worth while to consider the meaning of this phrase. So far as it possesses any definite meaning—for, of necessity, the term is an elastic one—the qualification implies “at such a price as a willing purchaser would be prepared to give.” That is to say, the assets should be written down from *W* time to time to effectively provide for depreciation. A fluctuation in value caused by external circumstances will, however, also require to be taken into consideration when property changes hands. It is important to remember that it is not really practicable to so maintain the efficiency of assets that no Depreciation shall ever occur, and also that private firms are under no statutory requirement to *retain* the whole of the undertaking intact. The Double-Account principle does not, therefore, apply to the accounts of private traders: it is, indeed, only suitable in cases where, owing to the *multiplicity* of assets, the expenditure on repairs and renewals in each year naturally and automatically approaches very closely to the actual loss by way of Depreciation.

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The accounts of what may be termed “registered” companies next claim attention. These companies, having a perpetual succession, are, perhaps, entitled to be considered theoretically permanent (although in practice, they are generally much shorter-lived than private enterprises), and consequently the Double-Account principle of stating values might be employed (but for the fact that a registered company is under no obligation to retain possession of any of its assets) if it were found practicable to say definitely what were, and what were not, fixed assets. This is a point upon which even Accountants might not always be agreed, while the recent statement of Lord (then Mr.) Justice FARWELL, in the case of *Bond v. The Barrow Haematite Steel Co., Lim.*, that blast furnaces owned by a smelting company must be regarded as part of its floating assets, emphasises the importance of a system of accounts which may be as independent as possible of any necessity of definitely distinguishing between fixed assets and floating assets. Incidentally it may be mentioned

that the terms most commonly used by lawyers, "fixed capital," and "floating (or circulating) capital" are clearly incorrect. The capital of a company is that which has been contributed for the purpose of enabling it to carry out the "objects" for which it was formed: it may be possible to say what assets have been acquired with that capital, but even then the assets and the capital are clearly separate entities.

In the great majority of cases there can be no doubt that the position of affairs can be more readily and clearly disclosed by a single Balance Sheet than by accounts kept upon the Double Account System. In the case of companies, however, there is a further point to be considered, namely, that there are increases which are not divisible profits, and losses which (as a matter of law) need not be made good before dividing profits in the form of dividend. The Profit and Loss Account must obviously be framed so as to show the divisible profits, and the question thus remains to be considered how profits and losses that do *not* affect revenue—or, to put it another way, capitalised fluctuations—are to be treated. As a matter of bookkeeping, it is clear that two courses are open. Either the capitalised items must be disregarded in the Balance Sheet by misstating the value of an asset or a liability, or some account must be raised to record the profit or loss that is not taken to Revenue. If the latter course be adopted, the accounts should be sufficiently clear to explain what has been done: in the former case, if the assets are over-stated it is also necessary that mention should be made of the fact, as the assets appearing in a single-account Balance Sheet are *prima facie* assumed to be stated at a reasonable valuation. If, however, a profit has been made which is not available for distribution, it is often considered unnecessary to modify the accounts so as to disclose the circumstance. This point, however, will be discussed more fully under the heading of "Secret Reserves." As a general rule, the amount at which *all* assets are stated in the Balance Sheet—except where a special statutory provision to the contrary obtains—should be regulated by the realisable value of

such assets on the basis of a going concern. It may, however, be added that there are certain classes of undertakings, in addition to those provided for by statute, to which the application of the Double Account System is not inappropriate—*e.g.*, mines, collieries, speculative syndicates, and other concerns of an essentially non-permanent character.

In practice, assets may generally be divided into two classes: (1) Those that represent Capital more or less permanently locked up, and (2) those that do not; the former may be named **FIXED ASSETS**, the latter **FLOATING ASSETS**.

VALUATION OF FIXED ASSETS.—The points to be borne in mind here are that Depreciation may reduce their value, and that Fluctuation may increase or reduce their value. So far as Depreciation is concerned, inasmuch as it has directly contributed to the profit earned, it is clearly an expense with which profit may be fairly charged. The only question is "How?" which will be considered in full under the head of Depreciation. On the other hand, Fluctuation is something altogether apart from trading profit and loss, being merely the accidental variation (owing to external causes) in the value of certain property owned, but not traded in: to carry the amount of such variation to Profit and Loss Account would be to disturb and obscure the ⁽¹¹⁾ results of actual trading, and so render comparison difficult, if not impossible. Moreover, as has already been stated, the Profit and Loss Account should be so framed as to show a balance which actually exists and is properly available for dividend. On no account, therefore, should the results of Fluctuations affect the Profit and Loss Account. Whether or not it is desirable that such Fluctuations should be revealed by the accounts *at all* will be fully considered under the head of **SECRET RESERVES**.

The actual cost of acquiring Fixed Assets (*e.g.*, stamps, conveyances, registration fees, &c.) is usually capitalised. This is not unreasonable, as such expenses are clearly an integral part of the cost price of such assets.

VALUATION OF FLOATING ASSETS.—It being the essential feature of these assets that the whole aim of the undertaking is to convert—or be able to convert—they into cash at the earliest possible opportunity, the element of immediate realisation is an important factor in their value. The only point to remember is that, while a manufacturing profit is earned only when the manufacture is completed, a trading profit is only made when the sale is completed. Neither profit must be anticipated, but it does not appear to be invariably essential that manufacturing profit should be held over until a sale has been effected. It may be added that, where a manufacture consists of several distinct processes, and separate accounts are kept of the manufacturing profit earned under each process, there seems to be no great objection to each process being considered as a separate manufacture, so long, of course, as the goods are readily saleable at the usual trade price.

With regard to what is a trading profit, a most ingenious argument was once advanced by Sir RICHARD WEBSTER (now Lord Chief Justice) before the late Lord (then Mr. Justice) FIELD (in *Horden v. Faulkner and others*), in which it was contended that the most scientifically correct method of valuing a stock-in-trade was to take it at selling prices, less the average trade profit; it being suggested that any profit realised in excess of the average was in reality a profit on buying, not on selling; and any profit realised less than the average a corresponding loss on buying. The argument passed muster at the time, appears to be plausible, and indicates a system that would doubtless prove very convenient in practice; but, unless the profit on different articles was very uniform, it would hardly be a safe one to adopt.

RESPONSIBILITY FOR VALUES.—A much-debated point is the extent of responsibility incurred by the Auditor in relation to the values set upon the assets of a company in the published accounts of the directors. The opinion arrived at in the Court of Appeal in *The London and General Bank* case

upon this most important point appears to be that the Auditor incurs no responsibility whatever so long as, after exercising reasonable care and diligence, he has honestly arrived at the opinion that the accounts are correct. It will be seen, however, that this decision in no way commits itself to the expression of any particular opinion as to the mode of valuation to be adopted. In this latter respect it is interesting to note that the draft Bill recommended by the Departmental Committee appointed to consider the question of Company Law Amendment by the Board of Trade in November 1894, required that the Balance Sheet of every company shall show (*inter alia*) "whether the assets are taken at cost price, or by valuation, or on what other basis they are stated, and whether any, and if so what, amount or percentage has been written off, and what other provision, if any, has been made for depreciation." This recommendation has not become law, but it is a very excellent practice to follow, notwithstanding, and has for many years past been adopted by some leading accountants.

The question of auditorial responsibility is fully considered in Chapter X.

VERIFYING EXISTENCE OF ASSETS.—Having settled a basis of valuation, the next thing would appear to be to obtain evidence of the existence of the assets enumerated in the Balance Sheet.

The evidence necessary in each class of assets would be as follows :—

LAND AND BUILDINGS : The title deeds of the property. Should the property be mortgaged the title deeds will, of course, be in the possession of the mortgagee, and an acknowledgment of this fact should be obtained from him or his solicitor, together with a statement of the amount due. Conversely, the verification of an asset represented by a mortgagee is the production of the title deeds and the mortgage deed. In the case of a second mortgage the title deeds will, however, be in the custody of the first mortgagee, and

here the Auditor will require to satisfy himself that such first mortgagee has received proper notice of the existence of a second charge.

In the case of Copyholds there will, of course, be no title deed to inspect. In place thereof a certified copy of the roll of the Lord of the Manor should be produced. The difference between Freeholds and Copyholds is much the same as the difference between Registered and Inscribed Stocks.

STOCK-IN-TRADE : The original Stock Sheets, signed by the stock-taker, calculator, checker, and manager. Most accountants would, in addition, consider it essential that the extensions and additions be re-checked by one of their own staff, and, further, require to be satisfied as to the soundness of the principle of valuation adopted.

The Auditor's liability in connection with the valuation placed in the accounts upon the amount of stock-in-trade was considered in *The Kingston Cotton Mills* case and *The Irish Woollen Co.* case, which are more fully dealt with in Chapter X. It may be pointed out at this stage, however, that the general effect of these decisions seems to be that, where the circumstances of the cases are not such as to arouse the suspicions of an ordinarily capable and diligent Auditor, he is justified in relying upon the valuation of stock-in-trade which has been submitted to him and certified to him by the Managing Director. In the first-named case, however, the Auditors had taken the precaution to state in their certificate that they accepted no responsibility for the valuation of the stock "which had been certified to them by the Managing Director," and as a matter of prudence it would no doubt be well for Auditors to always add this qualification. It may be added, however, that such a qualification as this would certainly not appear to save the Auditor, where he had reasonable grounds for doubting the valuation itself; whenever his suspicions have been aroused, it is absolutely necessary that the Auditor should thresh the matter out to the bottom.

INVESTMENTS IN STOCKS AND SHARES: The Auditor will require to have produced to him the scrip, certificate, bond, or other document, proving that the ownership of the investment in question is vested in his clients; and he should also require production of the broker's note, with a view to verifying the cost price thereof. In the case of Consols and other inscribed stocks no such certificate of ownership is furnished, and in these cases it becomes necessary to obtain a certificate that, upon the date of the accounts, such stock stood registered (or inscribed) in the names of the Auditor's clients. It is important to notice the *date* of such certificate, as it is not in itself a proof of ownership, but merely a record dealing with that particular date alone, and it differs from an ordinary certificate, or scrip, in that, in the event of a subsequent sale, it does not have to be given up.

Investments on behalf of a company sometimes stand in the names of individuals, who hold them in trust for the company. A proper declaration of trust, duly executed, should in all cases be produced to the Auditor.

The following is a list of Inscribed Stocks, under the headings of the Banks at which they are respectively transferable. Forms of application for certificates can be obtained on application at the various Banks; they must, however, be signed by at least one of the persons in whose name the Stock stands. A small fee is payable, the cost of which should be borne by the client. The Auditor should see that the request is made that the required certificate be forwarded direct to himself:—

THE FOLLOWING INSCRIBED STOCKS ARE TRANSFERABLE IN ANY AMOUNTS AT THE BANK OF ENGLAND:—

2¾ per cent. Consolidated Stock (Goschen's Consols), 1923 (2¾ per cent. until 5th April 1903; 2½ per cent. thereafter until redeemed).

3½ per cent. Annuities, 1894.

2½ per cent. Annuities, 1905.

2¾ per cent. Annuities, 1905.

Local Loans 3 per cent. Stock, 1912.

India 3½ per cent. Stock, 1931.

India 3 per cent. Stock, 1948.
 Metropolitan $3\frac{1}{2}$ per cent. Stock, 1929.
 Metropolitan 3 per cent. Stock, 1941.
 Metropolitan $2\frac{1}{2}$ per cent. Stock, 1949.
 Liverpool $3\frac{1}{2}$ per cent. Stock.
 Birmingham $3\frac{1}{2}$ per cent. Stock, 1946.
 Birmingham 3 per cent. Stock, 1947.
 Swansea $3\frac{1}{2}$ per cent. Stock.
 Hull $3\frac{1}{2}$ per cent. Stock.
 Wolverhampton $3\frac{1}{2}$ per cent. Stock.
 Nottingham 3 per cent. Stock.
 Manchester 1891 Redeemable Stock (3 per cent.), 1941.
 New Zealand 4 per cent. Consolidated Stock, 1929.
 New Zealand $3\frac{1}{2}$ per cent. Consolidated Stock, 1940.
 New South Wales 4 per cent. Stock, 1933.
 New South Wales $3\frac{1}{2}$ per cent. Stock, 1924.
 New South Wales $3\frac{1}{2}$ per cent. Stock, 1918.
 Queensland 4 per cent. Stock, 1915.
 Queensland 4 per cent. Stock, 1924.
 Queensland $3\frac{1}{2}$ per cent. Stock, 1924.
 Queensland $3\frac{1}{2}$ per cent. Stock, 1930.

THE FOLLOWING INSCRIBED STOCKS ARE TRANSFERABLE IN MULTIPLES OF £1 AT THE BANK OF ENGLAND:—

Eastern Bengal Railway "A" Annuity, expiring 30th July 1957.
 Eastern Bengal Railway "B" Annuity, expiring 30th July 1957.
 Eastern Bengal Irredeemable 4 per cent. Debenture Stock.
 Scinde, Punjaub and Delhi Railway "A" Annuity, expiring 31st December 1958.
 Scinde, Punjaub and Delhi Railway "B" Annuity, expiring 31st December 1958.
 East Indian Railway $4\frac{1}{2}$ per cent. Irredeemable Debenture Stock.
 Oude and Rohilkund 4 per cent. Debenture Stock, 1898.

THE FOLLOWING INSCRIBED STOCKS ARE TRANSFERABLE IN ANY AMOUNTS AT THE LONDON & WESTMINSTER BANK, LOTHBURY, E.C., THE PROCEDURE BEING THE SAME AS AT THE BANK OF ENGLAND:—

Cape of Good Hope 4 per cent. Inscribed Stock of 1883.
 Cape of Good Hope 4 per cent. Consolidated Stock, 1916-1936.
 Cape of Good Hope $3\frac{1}{2}$ per cent. Consolidated Stock, 1926-1949.
 4 per cent. Victoria Inscribed Stock, 1881-2-3-4-5.
 $3\frac{1}{2}$ per cent. Victoria Inscribed Stock, 1888-9.
 $3\frac{1}{2}$ per cent. Victoria Inscribed Stock, 1921-6.

3½ per cent. Tasmanian Inscribed Stock, 1920-40.
 Newfoundland Inscribed Stock, 1913-38.
 3½ per cent. Brighton Corporation Stock, 1946.
 Cardiff Corporation Stock, 1935.
 3½ per cent. Reading Corporation Stock.
 3 per cent. Reading Corporation Stock.
 4 per cent. Western Australian Inscribed Stock, 1911-31.

THE FOLLOWING INSCRIBED STOCKS ARE SIMILARLY TRANSFERABLE IN ANY AMOUNTS AT THE OFFICE OF THE CROWN AGENTS FOR THE COLONIES, 1 TOKENHOUSE BUILDINGS, E.C.:—

Western Australian (January and July 1934) 4 per cent.
 Natal 4 per cent. Inscribed Stock (April and October 1937).
 Natal 4 per cent. Inscribed Stock (May and November 1927).
 Natal 3½ per cent. Inscribed Stock.
 Ceylon 4 per cent. Inscribed Stock.
 Ceylon 3 per cent. Inscribed Stock.
 Jamaica 4 per cent. Inscribed Stock.
 Mauritius 4 per cent. Inscribed Stock.
 Mauritius 3 per cent. Inscribed Stock (guaranteed).
 Grenada 4 per cent. Inscribed Stock.
 Trinidad 4 per cent. Inscribed Stock.
 Hong Kong, 3½ per cent. Inscribed Stock.
 British Guiana 4 per cent. Inscribed Stock.

Funds deposited as security might be taken on the certificate of responsible persons, provided the deposit is itself clearly regular.

It may be added that if, when examined, the securities are securely sealed up in packages, it is not necessary at subsequent audits to re-examine them in detail, if the seals remain unbroken.

BOOK DEBTS.—The extent to which it is practicable to verify the existence of Book Debts depends largely upon circumstances. Unless they are very numerous the Auditor should satisfy himself that the total appearing in the Balance Sheet agrees with the Ledger balances, and that proper provision has been made for cash discounts and bad debts. With regard to the discounts, it is customary to deduct the full

cash discount upon all Ledger balances. It is questionable whether this is really necessary, although it is clearly a prudent course to adopt; but where cash discounts are deducted from the trade creditors they must, of course, be also deducted from the trade debtors. With regard to bad debts, the Auditor should obtain a certificate of at least one responsible person acquainted with the facts, to the effect that in his judgment due provision has been made for any loss that is reasonably likely to occur. It is naturally impossible for the Auditor to verify this provision in detail, but he can at least take note of overdue and "dead" accounts, and see whether such provision as appears to *him* to be adequate has been made in respect of these. As the number of Book Debts increases it becomes impracticable for the Auditor to verify the Ledger balances in detail; it has already been explained, however, that, where an adequate system of internal check exists, the verification of details can to a large extent be superseded by tests. For all practical purposes it is probably as efficacious to check the balances of, say, one or two Ledgers out of twenty as it would be to check the whole. The serious frauds which occurred some years since in connection with *The Millwall Dock Company* serve, however, to emphasise the importance of *some* tests of the accuracy of the Book Debts, even in the case of large undertakings where the number of Ledgers in use is enormous.

PLANT, MACHINERY, FIXTURES, &c.: There is, perhaps, too much tendency to assume the correctness of the "book" figures with regard to these assets, provided reasonable provision has been made for depreciation: it is important, however, to make careful enquiries into all additions, with a view to seeing that they represent *bona fide* capital expenditure that may properly be added to the value of the asset, and, further, to make particular enquiry as to the sale of worn-out or discarded assets. It not infrequently happens that such sales are erroneously credited to Sales Account, with the result that the latter is over-stated and that due enquiry into

the *loss* in respect of such sales is overlooked. The amount realised on the sale of fixed assets should, of course, be credited to the real account standing in the books in respect of this asset; but the realisation affords an opportunity of enquiring into the value at which these assets stood in the books, and should they have been sold at a loss, that loss must in all cases be written off, as otherwise an item will be brought into the Balance Sheet as an asset which represents assets no longer in existence.

Occasionally, as has already been stated, a re-valuation will be made for the purpose of assessing, or of checking, the provision for depreciation; but in any case a certificate should be forthcoming, to the effect that the various items included in the last inventory are still the property of the undertaking.

BANK BALANCE: Banker's Pass Book verified either by personal visit to Bank or by Banker's certificate of balance.

In practice it will rarely happen that the balance recorded in the Pass Book exactly agrees with the balance in the Cash Book, and a Reconciliation Account has therefore to be prepared upon the following lines:—

Balance as per Pass Book ..	£1,267	1	9
<i>Less</i> Cheques unpaid, viz. :—			
Dec. 16, Jones	£29	2	0
„ 21, Smith	16	5	9
„ 29, Brown	71	14	2
	<hr/>		
		117	1 11
		<hr/>	
		1,149	19 10
<i>Add</i> Payments in not credited, viz. :—			
Dec. 30, Bill No. 69 ..	£120	0	0
„ 31, Sundries	69	2	7
	<hr/>		
		189	2 7
	<hr/>		
Balance as per Cash Book ..	£1,339	2	5
	<hr/>		

Where practicable it is desirable that the Auditor should see that the various adjustments which constitute the difference between the Pass Book Balance and the Cash Book Balance

are rectified in due course by subsequent entries in the Pass Book.

In this connection the case of *The Brighton Eden and Empire Syndicate, Lim. v. London and County Bank, Lim.* (decided in 1904), will be found of interest. This was an action brought against the defendant Bank for damages for loss sustained through the negligence of their manager in allowing the manager of the plaintiffs to himself make entries in the Bank Pass Book, which entries were, it was stated, inaccurate in point of date although accurate as to amount. By this means the plaintiffs' manager was able for a number of months to avoid detection at the monthly audit of his accounts, and at the end of the year, when the defendant Bank were called upon to certify the balance shown in their Pass Book, the deficiency was made good, doubtless, by the plaintiffs' manager temporarily borrowing the amount of his defalcations. The decision in this case, that the defendant Bank were liable in damages, is satisfactory to Auditors, in that it makes a Pass Book duly obtained from a Bank a reliable basis for the Auditor's verification, whether formally certified as correct or not.

CASH IN HAND : Verified by production of actual cash balance, or, if the date of the accounts has gone by, by exhaustively verifying the Bank Account up to the date of audit and *then* counting the balance of cash in hand. In cases where there is more than one Cash till, all must be produced to the Auditor and verified by him simultaneously ; and, wherever practicable, it is preferable that all cash in hand should be paid into the Bank on the afternoon of the date of the Balance Sheet, in which case, of course, no occasion arises for the Auditor to verify the balance of cash in hand, for the all-sufficient reason that there is none. In the case of cash at distant branches a satisfactory certificate that the balance exists may generally be accepted in lieu of actual counting. In continuous audits all cash balances should be frequently verified, say, at least once a month.

In the case of *London Oil Storage Co., Lim. v. Secar, Hasluck & Co.* (*vide* Appendix "B") an unsuccessful attempt was made to plead that it was no part of an Auditor's duty to verify the balance of petty cash in hand. This might fairly be conceded if the balance of petty cash did not exceed the usual limit of about £5, but in the case in question the Petty Cash Book showed a balance which had gradually increased from £21 in 1897 to £796 in 1902. And whatever may be said in general terms, therefore, as to the desirability of an Auditor verifying balances of cash in hand, it is clear that it would be only prudent to regard the existence of a large floating balance as *prima facie* a matter for suspicion, and therefore a matter calling for careful enquiry; and this was the view taken by the jury in this case, although they only awarded the plaintiffs nominal damages.

BILLS RECEIVABLE: Verified by production of the actual bills themselves. Care should be taken to see that no overdue bills are included in a Balance Sheet under the heading of "Bills Receivable"; that due provision is made for discount where necessary; and that all anticipated loss by way of bad debts in respect of Bills Receivable—both in hand and under discount—is included in the accounts.

WORK IN PROGRESS: This should be certified by the Works Manager, the Chief of Cost Office, and the Managing Director. In the case of readily saleable goods manufactured in quantities the usual rule is to value work in progress at cost—the term "cost" being defined as the cost shown by the Cost Accounts, which as a rule includes, of course, a certain amount of "loading" for factory and other standing expenses. As has already been stated, when the work of any one manufacturing department has been completed, there seems no reason why that department should not be entitled to take full credit for the work performed; but in such cases care must, of course, be taken to see that the stock of unfinished goods represents items that will be finished and sold at the normal rate in due course.

When work in progress consists of single articles—as, for example, in the case of contract work—its valuation becomes both a more difficult and a more serious matter, partly because past experience is no longer available as a guide, and partly on account of the magnitude of the figures involved. In the case of contracts extending over a number of years it is clear that annual accounts can only approximately estimate the true net profit earned in each year. In the case of manufacturing firms it is for the partners to mutually agree a basis for the valuation of work in progress, but the safest course would appear to be not to take credit for any profit on uncompleted work. In the case of companies, however, which require to produce annual accounts, and to pay annual dividends, this course is hardly practicable. A company is not obliged to wait until profits have been actually realised in cash before crediting anything to Revenue. There is, therefore, no illegality in taking credit for estimated profit on work in progress; but, in view of the extreme difficulty of arriving at an accurate estimate, and the extreme uncertainty that often prevails as to what the ultimate result will be, it is clear that only very conservative estimates can be safely indulged in. Cost Accounts should, of course, in all cases be available to show the actual cost of each contract up to the date of the accounts. If the work has so far proceeded that it is possible for the Works Manager to certify an outside figure, that will not be exceeded, for the cost of completing the work, it would not be unreasonable to apportion the profit between the two periods according to the expenditure incurred in each, providing, of course, ample reserves in all doubtful cases. In connection with work less far advanced it seems more questionable whether anything in excess of manufacturing cost can be safely treated as an asset. In this connection, however, it may be borne in mind that all large contracts are readily capable of division into sections, the cost of each of which has already been estimated in advance. A comparison of the Cost Accounts in respect of the work performed with the original estimates will thus enable a very fairly reliable view to be obtained of the general position of the

contract, more especially, of course, in those cases where the speculative part of the work is in the earlier stages.

In the majority of cases, where contracts extend over a lengthy period, it is usual for payments to be made on account, upon the certificate of the architect, or superintendent engineer, as the case may be. The amount of such payments would be from 75% to 90% of the value of the work actually performed, and it is clear, therefore, that the excess of money received over expenditure incurred may safely be regarded as the minimum profit earned up to date.

An interesting discussion of this question took place at a meeting of the Chartered Accountants Students' Society of London on the 15th October 1902.

SALES FOR FUTURE DELIVERY.—The question has arisen more than once as to whether a company is entitled to take credit for profit expected to be earned in respect of orders booked for future delivery. The point is naturally one of considerable importance in some industries, as, for example, with wine merchants, who frequently book orders for future delivery, and also with regard to coal merchants, cotton merchants, and the like, who enter into contracts to supply their goods for some time in advance. The general rule which has been laid down in this work is, it is thought, unquestionably the safe one to in all cases adhere to, namely, that the profit on the sale of goods should be taken credit for at the time when the sale actually occurs; and where it is an essential portion of the contract of sale that the goods shall not be delivered until some future date, then the actual *sale* would certainly appear to be at the date of delivery, and not at the date of booking the order. Like many other matters, however, this is, perhaps, as much a matter of degree as a question of principle, and where orders have been actually booked, so that a valid contract exists upon which the customer could be sued for payment, the mere fact that the goods have not been delivered might well be overlooked and the profit taken credit for in the

period when the order was booked : this, however, could certainly only be applied where the goods were actually in stock, and not when they were still unmade. Even where it is decided that credit may reasonably be taken for such future sales, it is important to remember that when payment is delayed a reasonable rebate should be made for loss of interest, and under no circumstances could any harm be done by postponing the whole of the profit until the period when the goods were actually delivered.

OUTSTANDING ASSETS.—The point that now claims attention is the question as to how far it is the Auditor's duty to consider the propriety of including certain items among the assets that relate to transactions which, at the date of the Balance Sheet, are uncompleted.

It has been said that no profits should be taken into account that have not been actually received in cash, unless there is every reasonable likelihood that they will eventually be so received. This, of course, means that a sufficient provision must always be made for bad and doubtful debts, but it means something else besides. With some classes of transactions it is quite possible—even though the transactions themselves are not actually completed—to say with reasonable security what profit will eventually result ; and, in these cases, it would appear that the most correct course would be to apportion the profit so that each period took credit for the profit arising from its portion of the transaction. Thus, in the absence of evidence that would lead one to a contrary supposition, the profit arising from sales may safely be credited to the period in which the sales occur, and the profit arising from manufacture similarly belongs to the period in which the articles are manufactured. The income arising from first-class investments (*e.g.*, interest on Government Stock, or Railway Debentures, or rent receivable) may likewise be said to accumulate from day to day. With regard to the latter, however, the question of convenience intervenes ; and, unless the amount involved is of sufficient magnitude to render

absolute accuracy desirable, it would probably be considered sufficient if only those sums actually due were considered as assets—the amount accruing being taken as a set-off against liabilities of a similar nature, and a Suspense Account opened for the difference in a lump sum. Turning now to another class of transactions, the final result of which can only be approximately determined, no accruing profit can, with safety, be taken credit for upon the uncompleted voyages of ships, or uncompleted contracts (except in so far as previously indicated), not for accruing dividends upon *ordinary* shares in companies, nor (under normal circumstances) for uncompleted consignments; the eventual result of all these transactions being generally of so speculative a nature that it is not safe to do more than carry forward whatever expenses may have been incurred.

Sometimes, for the purpose of providing a Secret Reserve, assets are intentionally under-stated: except when done advisedly, however, there is but little fear of the Auditor finding the assets under-stated. Occasionally defalcations have, by this means, been made to fall upon revenue (generally by writing off good debts as bad), but the attention thereby attracted to the existence of a leakage prevents such a course from being at all common.

OUTSTANDING LIABILITIES.—For a similar reason, there is but little fear of liabilities being over-stated: how far it is necessary for the Auditor to take special steps to guard against their under-statement is the matter that now claims attention. While the practice of “dating forward” invoices is so common, there will always be some danger of goods being included in stock without having been passed to the credit of the Bought Ledger. “Stock-taking” statements might help to discover the omission, but they also might not. It will be a great help, therefore, if the services of the Stock-keeper are requisitioned, and he be made responsible for the production of invoices for all goods that have passed through his hands. The purchases for the next few weeks after the date of balancing may also be usefully scrutinised. Upon this point the decision of the

Irish Court of Appeal in *The Irish Woollen Co.* case is of interest.

All Expense Accounts (*e.g.*, wages, salaries, &c.) should be carefully examined, to make sure—as far as possible—that no outstanding liabilities have been omitted.

It is a common practice to set off accruing rent, interest, &c., against insurance rates, and other items paid in advance, and to keep a fixed sum suspended to meet whatever difference there may be. The plan certainly possesses the advantage of convenience combined with practical accuracy; but the sufficiency of the fixed sum should be verified at every audit, as the circumstances may easily vary from time to time.

The Auditor's own fee is a matter in which he will naturally be interested. There is no uniform practice, however, some preferring to debit the accounts of the period under audit with the fee, and some the period in which the audit is conducted. The latter course is naturally the most convenient where the amount chargeable depends upon the time occupied, but the former method is probably the more correct.

The Minute Book may disclose the existence of liabilities—both certain and contingent—that are not recorded in the books of account.

CONTINGENT LIABILITIES must not be forgotten. Bills discounted are perhaps the most usual source of contingent liability. Disputed claims must not be lost sight of, however; and claims for dilapidations upon premises, the lease of which has almost expired, should be anticipated, so that the whole loss may not fall upon one year. Arrears of Cumulative Preference Dividends also come under this heading, although some dispute this statement on the ground that preference shareholders have no absolute right to any dividend until it has been formally declared.

HIRE-PURCHASE AGREEMENTS.—This subject is of sufficient importance to merit a separate heading. In

former editions of this work its proper treatment was considered very exhaustively, because (so far as the author was aware) the principles underlying these transactions, and the best methods of applying them, had not then been treated in any other book. The detailed treatment of the subject has, however, now been transferred to the author's *Advanced Accounting*, which deals fully with those advanced problems that are questions of account, as such, rather than questions of auditing.

From the Auditor's point of view the main point of importance is to see that a correct system of dealing with the transactions is adopted which charges a sufficient proportion of the instalments against the revenue of each year, so as to avoid the proportion which is being capitalised appearing at too high a figure. This is a pure question of interest calculations, and the following Table will suffice to show the present value of the unpaid instalments upon any hire-purchase agreement for the acquiring of railway wagons.*

TABLE SHOWING PRESENT VALUE OF PAYMENTS UNDER
HIRE-PURCHASE AGREEMENTS.

Instalments : £100 per annum	At 5 per cent. Yearly Rests	At 5 per cent. Half-Yearly Rests	At 6 per cent. Yearly Rests	At 6 per cent. Half-Yearly Rests
	£	£	£	£
Agreement with 1 year to run	95'238	96'371	94'340	95'673
" " 2 " "	185'941	188'098	183'339	185'855
" " 3 " "	272'325	275'406	267'301	270'859
" " 4 " "	354'595	358'507	346'511	350'984
" " 5 " "	432'948	437'603	421'236	426'510
" " 6 " "	507'569	512'888	491'732	497'700
" " 7 " "	578'637	584'545	558'238	564'803
" " 8 " "	646'321	652'750	620'979	628'055
" " 9 " "	710'782	717'668	680'169	687'675
" " 10 " "	772'173	779'458	736'009	743'674

The amount charged against Revenue must be equal to the interest on the present value of the instalments due at the commencement of that period, and the apportionment must be so arranged that when the agreement expires the proportion

* In cases where a reference to Tables is impracticable the Auditor will be upon the safe side if he reckons the Cash Value as being the aggregate amount of the instalments minus simple interest thereon, at the prescribed rate, for half the prescribed period.

that has been capitalised does not exceed the present value of the instalments at the date of the commencement of the agreement. All repairs must, of course, have been charged to Revenue, and some further provision must be made for Depreciation. This, however, may be more conveniently discussed under that heading.

The above remarks apply in their entirety to hire-purchase agreements for the acquiring of railway wagons and any other articles which are ordinarily purchased upon such terms that the rate of interest is either 5 per cent. or 6 per cent. At the present time, however, cases frequently occur in which FURNITURE, MUSICAL INSTRUMENTS, BICYCLES, &c., are sold under hire-purchase agreements, and in these cases the rate of interest charged is almost invariably far higher, usually varying from 10 per cent. to 30 per cent. per annum on the unpaid instalments. The proper treatment of these transactions is fully considered in the author's *Advanced Accounting*: for present purposes it will be sufficient to point out that firms transacting business of this description in the nature of things deal with a very large number of items, each of comparatively small amount. It consequently follows (1) that it is impracticable to keep such intricate accounts as would be necessary to accurately apportion every instalment received between interest and capital; (2) that such scrupulous exactness is unnecessary in practice, as the volume of the transactions is sufficient to enable an *average* to produce fairly reliable results. The best principle, therefore, is to regard the difference between the cash price and the credit price of the articles sold as interest charged, and having ascertained the average rate of interest to apportion it between the three years over which the currency of these agreements almost invariably runs. By this means practically accurate results can be obtained with a very small expenditure of labour. The apportionment should, however, be in favour of the later years, so as to err upon the side of caution, and it may be added that the provision for Bad Debts will here require special consideration.

DEPRECIATION.—The importance of this question is considerable, and it is therefore desirable that the matter should be considered in detail. Before doing so, however, it may be well to remind the reader of the distinction between Depreciation and Fluctuation. Depreciation is a shrinkage in value which, in the ordinary course of events, may be expected to take place, as being a necessary consequence of the possession and enjoyment of the asset : it consequently is a charge against Revenue. Fluctuation, on the other hand, arises from causes entirely outside the scope of the business, and may affect the value of its assets either adversely or favourably. The operations of Fluctuation cannot, however, affect true trading profits either one way or the other, and as a rule, therefore, it is best to disregard it in the accounts. A favourable Fluctuation in the value of fixed assets seems the proper subject for a Secret Reserve. A favourable Fluctuation in floating assets is temporarily a Secret Reserve, which will be included in the trading profits when those assets are realised. An unfavourable Fluctuation in floating assets may be disregarded so long as there is every reason to believe that it is of a temporary character, but if it seems likely that conditions will remain unfavourable until the time comes for realising those assets, then the loss should be anticipated ; or, to speak more accurately, it should be charged against the period in which it actually occurred, rather than against the period in which it was realised. An unfavourable Fluctuation in fixed assets need not, under normal circumstances, be charged against Revenue before declaring dividends out of current profits. It may therefore be disregarded in the accounts ; but, in order that the true position of affairs may be placed before the shareholders, it is desirable that either a note should be appended to the Balance Sheet, drawing attention to the shrinkage in value, or a paragraph to that effect be inserted in the Auditor's Report.

In connection with this distinction between Depreciation and Fluctuation it should be added that in some quarters the practice has been strongly advocated of occasionally having

fixed assets revalued as a check upon the annual provision for Depreciation. There is much to be said in favour of this view, in that it is always desirable to take every reasonable opportunity of testing the sufficiency of estimated provisions; but, on the other hand, it must be borne in mind that a re-valuation can hardly fail to take into consideration Fluctuation as well as Depreciation, and consequently may introduce into the accounts a disturbing element, obscuring the real result of the trading. It ought not, however, to be impossible to check the provision made for depreciation by means of re-valuation without introducing these complications.

In order to make it quite clear what is intended, it may be pointed out that a machine costing (say) £100, and a further £20 to fix, may answer its purpose for (say) six years, and then have to be sold as second-hand for £15. This leaves a cost of £105 to be written off over the six years' life. Under the circumstances it might be reasonable to charge this at the rate of £17 10s. od. per annum (equals $14\frac{1}{2}$ per cent.), or the efficiency of the machine may be so high when new that the reasonable procedure would be to charge $27\frac{1}{2}$ per cent. on the reducing balance, which would reduce the £120 to (approximately) £15 at the end of the sixth year; but, whichever method be adopted, it is more than probable that the balance shown on the Machinery Account at the end of the first, second, third, fourth, and fifth years would not agree with the valuation made by an expert at those times. The reason for this is that the expert would take into consideration the value of the machine in the market, whereas the manufacturer is only concerned with its value to him. Moreover, the market value may be influenced by other considerations besides the actual condition and state of newness of the article in question. The existence of new and better types is, of course, a risk that ought to be provided for by Depreciation, but fluctuations in the value caused by an increase or reduction in the *cost of producing* similar machines in no way affect the cost of the original machine that has to be written off over a term of years.

COMPARATIVE TABLE.

				Reduced by 14½ % on Cost	Reduced by 27½ % per annum	Re-valued (say)
Cost (including Erection)	..	..	..	£ 120'00	£ 120'00	£ 120'00
Depreciation 1	..	..	..	17'50	33'00	40'00
				102'50	87'00	80'00
" 2	..	..	..	17'50	23'92	15'00
				85'00	64'08	65'00
" 3	..	..	..	17'50	17'60	15'00
				67'50	46'48	50'10
" 4	..	..	..	17'50	12'78	10'00
				50'00	33'70	40'10
" 5	..	..	..	17'50	10'18	10'00
				32'50	23'52	30'00
" 6	..	..	..	17'50	6'47	15'00
Estimated Break-up Value	..	..	..	£15'00	£17'05 *	£15'00

* The estimate is (it will be seen) too large. It is, however, no serious matter to charge the whole of the deficit—£2'05—against the sixth year's profits, increasing that charge to £8'52.

With these preliminary remarks we may proceed to the special features in connection with the depreciation of various classes of assets to be considered.

FREEHOLD LANDS may quickly be dismissed—they suffer no depreciation. Fencing, and other similar works, would, of course, depreciate, but the item would not usually be of sufficient importance to require consideration. If, however, it became a large item, it should be treated separately as Plant (*q.v.*).

FREEHOLD BUILDINGS depreciate to an extent varying greatly according to the quality of the workmanship and materials employed in their erection. The amount of the Ledger Account will frequently include freehold land, which, as we have seen, does not depreciate; the depreciation will therefore be confined to the building itself. If the *Instalment* plan be adopted, from 1¼ to 3 (or even 5) per cent. of the original amount may be deducted annually; if the *Annuity* method be used a fixed sum debited to Revenue, which, after

crediting interest, will write the asset down to zero in from, say, 50 to 150 years; or, if the Sinking Fund system be preferred, such a sum may be set aside as will accumulate to the cost of the building in that time. In each case all repairs will have to be borne by Revenue, in addition to the depreciation. With regard to the relative merits of the Instalment, Annuity, and Sinking Fund methods, the two latter are distinctly preferable; although—on account of its greater simplicity—the Instalment method is frequently used for short leases. The Annuity system differs from the Sinking Fund in that the instalments are not invested; the (net) amount of each successive instalment therefore requires to be increased to compensate for loss of interest on the previous uninvested instalments. Tables showing how the amount of such instalments may be arrived at will be found at the end of this work (*vide* Appendix “D”).

GOODWILL does not “depreciate.” On the other hand, it will generally be conceded that it is liable to fluctuations, both continual and extreme; as, however, no one would think of calling its omission from a Balance Sheet a Secret Reserve, it will probably be most convenient to deal with the question of Goodwill under the present heading. As a matter of fact, Goodwill is not written down *because* its value is supposed to have become reduced—such a course is all but unknown. The amount at which Goodwill is stated in a Balance Sheet is never supposed to represent either its maximum or its minimum value; no one who thought of purchasing a business would be in the least influenced by the amount at which the Goodwill was stated in the accounts; in short, the amount is absolutely meaningless, except as an indication of what the Goodwill may have *cost* in the first instance. Inasmuch, therefore, as nobody can be deceived by its retention, there is no *necessity* for the amount of Goodwill Account to be written down. On the other hand, the practice is not unusual, where sufficient profits are being made. The question is not, however, one upon which the Auditor is required to express an opinion; and, so long as the item is separately stated on the Balance Sheet, it is scarcely

desirable that he should interfere with the discretion of the management, although there is, of course, no objection to his offering an opinion when he is invited to do so.

HORSES invariably depreciate, and—if heavily worked—very rapidly. The rate of depreciation will probably vary between 15 and 25 per cent. on the starting balance of the account. Until experience has shown the actual rate of depreciation it will be safer to arrive at the result by a re-valuation (which, with horses, can be more accurately done than with most things), and where only a small number of horses are employed (say 20 or less) the re-valuation should often be resorted to, if only as a check upon the rate of depreciation employed.

INVESTMENTS need not be depreciated unless of a wasting nature—such as shares in Mines or Single-Ship Companies. As to how far it is desirable that fluctuations in their value should be considered, the reader is referred to the paragraph on Secret Reserves (*postea*).

LEASEHOLD LAND AND PREMISES.—The premium paid for leases may be regarded as the purchase-money paid for a terminable annuity of the difference between the annual value of the property and the annual charges. In short-term leases the readiest method will be to charge a proportionate part of the term against each year's Revenue; but the method is too rough to be employed if the term exceeds, say, eight or ten years. In the case of longer leases the Annuity, or Sinking Fund, plans, which were discussed under the heading "Freeholds," should be adopted. Almost invariably the termination of a lease finds the late lessee liable to a heavy claim for dilapidations; this claim will frequently amount to one year's rent, or even more, and it is therefore a convenient and prudent course to adopt to deduct about one year from the unexpired term of the lease before making the depreciation calculations. All repairs are, of course, chargeable to Revenue; but they may be averaged by the temporary or permanent employment of a Repairs (Fund) Account through which

Revenue is charged with a fixed amount annually, the difference between the actual expenditure and the annual charge being brought forward as a liability, or (more rarely) as an asset.

Before leaving this point it is well to bear in mind that, in the case of exceptionally long leases, or exceptionally badly built premises, it may be necessary to increase the annual charges for depreciation beyond the usual rate, so as to provide for the rebuilding of the structure during the lease.

LICENSED HOUSES present some rather special features. The goodwill attaching to the licence gives the lease or freehold of licensed premises a market value greatly in excess of the real value of the buildings. A licence on freehold premises does not depreciate, but a licence on leasehold premises passes away with the premises, and must therefore be depreciated like a lease. A licence may at any time be withdrawn—either for misconduct or for no reason—but this is a contingency outside the scope of depreciation. It may, however, be provided against by insurance, which would appear to be a most prudent course to adopt.

MACHINERY depreciates by wear and tear and by becoming obsolete. In addition to charging all repairs and (partial) renewals to Revenue, from $7\frac{1}{2}$ to $12\frac{1}{2}$ per cent. should be written off annually from reducing balances. Boilers, which depreciate more rapidly, should be reduced from 10 to 15 per cent. per annum. Loose tools are most conveniently dealt with by means of a re-valuation. It is desirable that a sound practical opinion be obtained as to the precise rate to be adopted in any particular case, and a thorough re-valuation from time to time is very desirable.

MINES undoubtedly depreciate in direct proportion to the amount of mineral extracted. By a singular inconsistency of the law, however, no depreciation need be provided for by a mining company before declaring a dividend. Where depreciation is provided the correct method appears to be to write

off annually such proportion of the total cost (less residual value of plant) as the year's output bears to the estimated contents of the mine, or—in the case of a lease—such proportion of the total cost as the year's output bears to the estimated total output during the lease.

On the other hand, it must not be forgotten that there is so much uncertainty about mining ventures that it would be practically impossible, merely by the adoption of any system of accounts, to ensure that the whole of the Capital of the undertaking was always maintained intact; while the persons who invest in this class of concern would doubtless object to large funds accumulating in the hands of directors, and earning a low rate of interest, which might legally be distributed as dividend, even though in point of fact they constitute a return of Capital. Perhaps, therefore, it is best that mines should be regarded as coming under a distinct category as "non-permanent" undertakings, the excess of current income over current expenditure being distributed, irrespective of the value of the remaining assets as contrasted with the paid-up capital.

It has already been stated that the "Cost Book" system appears to be one of the most suitable for mining industries, and it may be added that this system—with but slight modifications to meet purely local requirements—is very generally adopted throughout Australia, where almost all the companies registered locally for mining purposes are registered as "no liability" companies. These companies are without fixed capital, the working capital required being obtained by calls on the members, who, however, have at all times the right to forfeit their membership, and upon so doing incur no further liability whatever.

PLANT, other than machinery, generally runs comparatively little risk of becoming obsolete, and a deduction of from 5 to $7\frac{1}{2}$ per cent. will therefore usually suffice. FURNITURE and FITTINGS should, however, be subjected to a somewhat higher rate. In both cases an occasional re-valuation will be desirable.

PLANT (or MACHINERY) acquired upon the HIRE-PURCHASE SYSTEM must, of course, be depreciated. Under normal circum-

stances the depreciation will be in accordance with the nature of the asset, whatever it may be. It should be borne in mind, however, that if full Depreciation be charged during the currency of the agreement, in addition to the proper interest instalments, the consequence will not infrequently be to charge against the profits of the earlier years a sum in excess of what it would have cost to merely hire the articles in question. The cost of simple hire may fairly be regarded as the maximum amount that need ever be charged against profits for the use of any asset, consequently the full provision for Depreciation may require to be modified during the currency of the hire-purchase agreement.

PATENTS are virtually leases of a monopoly, and although it is possible that some value—in the nature of goodwill—may remain after the patent has run out, it seems desirable that the cost of a patent should be written off within the course of its life. Renewal fees seem to correspond to ground rents. Where a patent has not been purchased, but remains the property of the original patentee, it is very undesirable that the item should be treated as an asset at all, except to the extent of its actual cost in fees, &c.: such a course would seem to be every bit as artificial as a similar treatment of goodwill, which *sans dire* is a latent asset in every paying concern.

The late Mr. A. A. JAMES, F.C.A., has, however, expressed the opinion that patents should not be written down, but that a general Reserve should be built up *per contra*. When the patents represent the bulk of the assets—and the undertaking is thus essentially “non-permanent”—this would, upon the whole, appear to be the best course to adopt.

A similar mode of treatment will apply to COPYRIGHTS, except that their commercial value has usually expired long before the copyright has run out. (*See further under “Publishers’ Accounts.”*)

SHIPS undeniably depreciate, although the rate at which they do so is so variable that no general rules can be given that would

prove of any practical utility. The amount of depreciation is usually certified by a competent engineer, and therefore—so long as his report looks plausible—the Auditor is relieved from undue responsibility. As already stated, it is almost unknown for a Single-Ship Company to provide for depreciation, it being inadvisable to allow a large depreciation fund to accumulate in the manager's hands. So long as the Auditor's certificate makes it perfectly clear that no depreciation is being laid aside, and so long as the Courts see no illegality in such a course, there does not appear to be any valid objection, from an Auditor's point of view, that is not outweighed by the resultant advantages. A Single-Ship is obviously a "non-permanent" undertaking.

THEATRICAL PLANT, &c.—Although there can be no reasonable doubt that theatrical scenery, "props," and other stock-in-trade are liable to depreciation, it is probable that few accountants would care to accept the responsibility of settling the actual amount. So far as the author has been able to ascertain, there is no uniform practice in vogue; but a periodical re-valuation appears to be adopted in many cases, and will very likely recommend itself to the Auditor as being perhaps the safest course. COPYRIGHTS and PERFORMING RIGHTS, when not purchased upon "sharing" terms, will also require to be dealt with; but, unless there appear to be very good reasons for believing that a "Revival" at no very distant date would prove remunerative, it would probably be considered safest to regard the whole cost as a mounting expense. Unless the Auditor is acting on behalf of a company or a creditor, the best plan will, no doubt, be to leave the whole question to his client's discretion.

REPAIRS will, in all cases, require to be charged against Profit and Loss; but, with a view to equalising profits, it is a very good plan to charge a fixed sum to Profit and Loss, and to credit that sum to a "Reserve for Repairs Account," against which account the actual repairs will be debited. Except in very special cases, however, a debit balance on the Reserve Account should not be passed as an asset. If the amount expended upon

repairs is below the average of previous years it may be desirable to reconsider the value of the property itself.

LANDLORD'S FIXTURES.—In the case of plant, machinery, and fittings erected upon leasehold property, it is important not to lose sight of the fact that, so far as these become landlord's fixtures, the minimum rate of depreciation permissible is one that will entirely write off the book-value by the time the lease expires. The question as to what are, and what are not, landlord's fixtures is, however, far too intricate to be usefully dealt with here; so long as the principle is borne in mind the determination of the question of fact may be left for the Auditor to deal with in each case as it arises. If there be any real doubt, a competent legal opinion should be sought.

THE LATE MR. ADAM MURRAY'S VIEWS.—The general question of Depreciation is one of such great importance that the views of so experienced an accountant as the late Mr. ADAM MURRAY, F.C.A., can hardly fail to prove of very considerable interest. Mr. MURRAY delivered a lecture upon "Wear and Tear and Depreciation," at Liverpool in 1887, which is (by special permission) reproduced below.

"In submitting a short paper on the above subject it is intended only to offer some general remarks; to give a few cases in illustration, and to refer to others upon which a difference of opinion exists.

"At the outset it will be convenient to make a distinction between Wear and Tear and Depreciation. Depreciation is a comprehensive term, including wear and tear; but the two are distinct elements, and may be considered separately.

"*Wear and Tear* may be defined as 'diminished value arising from use,' as in the Income Tax Act 1878, 41 Vict., cap. 15, section 12, under which a deduction was for the first time allowed in the assessment of profits under Schedule D, such allowance being in respect of 'diminished value by reason of wear and tear.' Although described in the Act to be for 'wear and tear,' yet in the form of Income Tax

Return No. 11a, under Schedule D, the word 'depreciation' has been adopted; still, the Income Tax Commissioners and Surveyors limit the allowance to wear and tear.

"The word 'depreciation' is almost universally used in the deduction from Property, Plant, and Machinery Accounts, and the corresponding charge made to Profit and Loss Account, but in the case of most ordinary trading concerns 'wear and tear' might properly be substituted for 'depreciation.'

"Under the head of 'wear and tear' it is proposed to deal with the ordinary charge made in Trading Accounts for the use of buildings, machinery, and plant.

"It is equally an item in calculating the cost of production, as is the payment for labour and for materials consumed.

"In ascertaining the cost of materials and stores used, the stock is taken at the end of the period against the stock at the beginning, and purchases during the period, the difference being the consumption.

"In the case of buildings and machinery a deduction is made, but the effect is the same as taking the property and plant into stock at a reduced amount, or at an increased amount if the additions during the period have been in excess of the deduction for wear and tear.

"Although the process differs, yet the result attained is the same, the cost of materials used being *ascertained*, the charge for the use of buildings and machinery being *estimated* without reference to change in value from other causes than use. It would not be a safe basis to take the value, as there is a fluctuation in the value of buildings and machinery irrespective of use.

"In order that the cost of production should be approximately correct for the purpose of fixing the selling price, or for comparison with the market price, it is important that wear and tear should neither be over nor under-estimated. For instance, the cost of building a cotton mill and furnishing it with machinery may some years ago have been equal to 30s. per spindle. Such a mill may now be built fully equipped with machinery having all the latest improvements at about 20s. per spindle.

In the case of an old mill it would be misleading to charge more for wear and tear than would be sufficient in the case of a new mill, consequently an old mill, unless it had been written down in the books at a high rate for wear and tear, might stand at a sum relatively higher than that of a mill built in more recent years.

"On the other hand, in the times of large profits (now passed away) it was not unusual to write off altogether the cost of the mill and machinery, or to reduce it to an amount much below the value. In such case the element of wear and tear might be lost sight of, or underestimated, and thus the spinner would be deceiving himself as to the cost of production.

"In the present days of bare profits it is of the utmost importance that the cost should be fairly estimated, and the mill proprietor should look at the question of wear and tear between himself as a landlord on the one hand and as a tenant on the other.

"It is not unusual in the cotton manufacturing districts for a manufacturer to rent a weaving shed with looms and power at an annual rent of so much per loom, and an owner occupying his mill should in like manner charge his business with a rent equal to interest on the value of the buildings and machinery, together with a charge for wear and tear beyond the cost of repairs, renewals, and maintenance, the outlay in respect of which should be debited to the Trade Account as part of the ordinary expenses.

"Much confusion and uncertainty exists in the Property and Machinery Accounts of many manufacturing businesses, by reason of the way in which wear and tear and renewals are treated. It is not unusual to make a deduction from the Property Accounts for wear and tear, and then to add to those accounts the outlay not only in the nature of additions and extensions, but also for renewals; the result not unfrequently being that the Property Account is upheld at a sum far beyond its real working value, and as a consequence the profits are apparently more than the actual profits. A safer course, in my opinion, is to make a deduction from the property for wear and tear, charging such deduction to the Profit and Loss Account, as well as the entire cost of maintenance, thus increasing Property, Machinery, and Plant Accounts only by the actual additions thereto.

"The accounts of railway companies and gas companies are kept on this principle, with this difference, that there is not any charge for wear and tear beyond maintenance, it not being required in the statutory form of accounts for those companies that there should be any such charge, and consequently in the Revenue Account actual maintenance is included only.

"In the case of railway companies owning steamships, there is a charge which is called 'depreciation,' but it would be more correctly described as 'provision for renewal of steamships.'

"Some municipal corporations owning gas works have exceeded their powers in charging the Profit and Loss Account with wear and tear

where there is not any such requirement in the special Acts conferring borrowing powers for gas works purposes, and the ratepayers are thus placed in a less advantageous position than that of shareholders of a gas company, in addition to which a Sinking Fund has also to be provided out of the gas profits of a municipal corporation.

"In making a deduction for wear and tear it is the practice with the majority of companies to follow the course usual with private trading concerns.

"Some, however, do not take wear and tear into account beyond the actual outlay.

"If it is objected that the cost of maintenance and renewals over a number of years may be unequal, this difficulty is met by estimating what amount annually is likely to be required for such purposes, and by charging the Profit and Loss Account with such amount, carrying the same to the credit of a 'Renewals and Repairs Account,' debiting the outlay from time to time to such account.

"It is not proposed to suggest what the rates for wear and tear should be in various businesses. These must be estimated by those conversant with and able to judge from practical knowledge of each particular business. It is sufficient to lay down what is believed to be a sound general principle, *i.e.*, to maintain existing works and plant out of revenue, and in addition to charge Profit and Loss with a deduction from property, machinery, and plant in respect of wear and tear.

"It is customary to make the deduction by a percentage rate from the cost *as reduced from time to time*, and not from the original cost. There is thus a larger amount for wear and tear charged in the early years, but the practice is preferred, seeing that in the later years, when the charge for wear and tear is less, there will be an increased expenditure for repairs and renewals as the unexpired term becomes shorter.

"If the life of an article, subject to wear and tear, was a known quantity, then the question of charge would be simplified. In such case interest would have to be added to the cost and balance cost, from year to year, writing off an annual sum to the Trading Account, by which cost and interest would be either extinguished altogether, or reduced to the value of old material at the end of the term.

"Let us now look at depreciation as distinguished from wear and tear; as the converse of appreciation, and as a separate element.

"Numerous and varied cases will suggest themselves.

"In addition to ordinary wear and tear, manufactories and works are subject to depreciation arising from

"(a) Improvements by which machinery may become of little more value than that of old material.

"(b) The less profitable state of trade.

"(c) The reduced cost of labour and materials.

"Where a manufacturer occupies his own property (as is almost invariably the case) as a prudent man he ought to have a reserve taken out of profits for these contingencies.

"It is an excellent plan to have an inventory of principal machines, tools, &c., kept in such a way as to show wear and tear deducted, as well as the reduced cost, in detail. By this means, if part of the machinery becomes superseded and has to be realised, the loss is readily ascertained and can be charged to Contingent Fund. This is not a merely theoretical system, but is in actual practice; of course, in such a case the loss or difference having been written off, any substitution would be chargeable to Plant Account, as in the case of an addition. Such an inventory would be of great use, as affording the means of making a comparison between the reduced cost of machinery as in the books, and the then working value.

"The proprietor of a mill or works built twenty years ago would find that as between himself as landlord and as a tenant he would now have to charge himself with rent only on the reduced value, and the difference between the present value and the cost would be a loss of capital and not a loss as a trader.

"It may be considered refining too much to make this distinction, still it is a convenient rule to apply, and assists in arriving at the correct principle in cases which frequently arise.

"Another case which properly comes under the description of depreciation is that of a leasehold property. If land is held under lease for twenty-one years, to be surrendered at the end of the term with the property upon it, the amount paid to the lessor and the cost of buildings erected by a lessee with interest thereon can be dealt with without any doubt as to the correct principle in such case, the term being fixed and not uncertain as in the case of machinery.

"Let us suppose that the land for the term of lease cost .. £1,000

"and the buildings erected by the lessee 2,500

£3,500

"If the lessee occupies the property for the purpose of his business he has to charge his trading with an annual rent, which he will ascertain in the following manner, the value of money being taken at 5 per cent. We find from one of Inwood's tables that the amount of £1 with

interest at 5 per cent. for twenty-one years would be £2,786, therefore the amount for £3,500 would be £9,751. Then we see from another of the tables that £1 per annum at 5 per cent. would in twenty-one years amount to £35,7193; then as £35,7193 : £9,751 :: £1 : £273, thus giving the annual rent or instalment as £273.

"If the land had been leased at £50 per annum then the charge to the business would be the rent and the annual instalment to write off the £2,500 (the cost of the buildings) and interest. In either case the annual charge is equal to the rent between the proprietor as a landlord and as a tenant. A Ledger Account of the cost, interest, and instalments, with annual rests, would, of course, be closed by the last instalment.

"Another case which comes within the experience of many of us is that of a colliery.

"A field of coal is leased, say, for thirty years subject to royalty on coal as it is won. The lessee expends on 'Sunk Capital Account' £100,000, in opening up and sinking pits. The charge to the Profit and Loss Account, in addition to the royalty on the coal, will be the annual instalment to be written off in the same way as in the previous case.

"Taking money at 5 per cent. the £100,000 would in thirty years amount to £432,190, £1 per annum at the same rate would amount to 66,4388; then as 66,4388 : £432,190 :: £1 : £6,505.08, this being the annual charge to be made by the lessee in his Profit and Loss Account as the annual rent which would be charged to him had the outlay been made by the lessor, he being content to have his expenditure back in thirty annual instalments, including principal and interest.

"The effect of wear and tear or depreciation taken out of the profits of a business is, of course, to increase the balance of floating assets over liabilities, or to reduce the excess of liabilities over floating assets, and it may not be unsuitable to refer to the proper application of money arising therefrom.

"In the case of works mortgaged, or advances by bankers or others, it would, of course, be wise to reduce any such liability. If there were not any such claims to meet, then it would be well to take the money out of the business rather than expend it in additions or extensions.

"A common error has been to use available funds of this kind for the purpose of building additional works or factories instead of investing the money to meet the cost of substitutions. When such time arrived there had been years of bad trade, and thus the means were not forthcoming, the consequence being embarrassment, if not ruin.

"And now a few observations as to Accounts and Balance Sheets in relation to the subject under consideration.

"As a means of affording information to those interested, it is desirable that wear and tear and depreciation should be shown as a deduction from time to time in the Balance Sheets of all trading concerns in the same way that additions to property and plant are usually set forth. In exceptional cases the error is made of having a Depreciation Account as a *fund* on the debit side of a Balance Sheet; the usual practice, however, being to charge wear and tear and depreciation against profits and to reduce the Property or Machinery Accounts correspondingly. It is misleading and erroneous to look upon such an entry in the Balance Sheet as a *fund* represented by assets. The property and machinery being of less value ought to be written down. The amount of wear and tear or depreciation is, no doubt, represented by money if taken out of profits; but it is only a change between fixed and floating assets, the latter being correspondingly increased.

"It is not usual to charge Profit and Loss Account in anticipation of wear and tear or depreciation, and so create an actual fund; but if such be the case it would be more intelligible if any transfer of the kind was made to the credit of such an account as 'Renewals and Repairs Account.'

"It has from time to time been suggested that there should not be any deduction made from profits for depreciation, but that it should be left to partners and proprietors to decide for themselves how much of the profits or dividends is in respect of interest, and how much principal.

"There appear to be several objections to such a mode of dealing with the accounts of trading concerns, although in some cases it is the practice.

"In the case of property, machinery, or plant subject to depreciation, such as:—

Manufacturing concerns,
Leasehold colliery,
Steamship company, &c.,

the Balance Sheet would be misleading, inasmuch as the capital of the company would apparently be represented by property and assets, when, in fact, they had greatly depreciated, and in some cases would cease to be of any value whatever.

"In a company, the shares of which had not any Stock Exchange quotation, and where sellers and buyers had to arrange prices between

themselves, intending purchasers would not have the means of satisfying themselves as to the value of the shares.

"It is not sufficient to say that existing shareholders are aware that part of the share capital is being repaid while outsiders would be in ignorance thereof. Dividends in such cases (consisting of both principal and interest in uncertain amounts) would not be any criterion of value.

"Directors generally would not approve of such an anomalous and objectionable mode of making up the accounts of their company.

"Accountants would hesitate, or indeed refuse, to sign such a Balance Sheet, inasmuch as it did not 'represent the true position of the company.'

"Having had experience of wear and tear and depreciation in various forms, their influence should be used to secure adequate deductions in order that Balance Sheets may be accurate, so that objection could not be taken to them.

"It would be most unsatisfactory and dangerous if property and assets were not written down, money arising from depreciation being applied in discharge of liabilities, or in reduction of share capital.

"It is greatly to be feared that in many cases where machinery (from the speed at which it is run) is subject to a high rate of wear and tear, sufficient allowance is not being made, and that, consequently, dividends include some portion of the capital where the shareholders are under the belief that they consist of profits only.

"Such a theory as has been suggested would, if recognised, lead to much inconvenience in the case of trust estates where there were life interests. Trustees could not be expected to take the responsibility of making a division of dividends between life-tenants and those entitled in remainder, and it would be most unsuitable to leave them in a position of having to decide how much should be considered income, and what portion a repayment of principal.

"We now come to the conclusion of a paper in which the intention has been to deal with a few leading features of the subject under consideration, including the following:—

"The distinction between Wear and Tear and Depreciation.

"The deduction from Buildings, Machinery, and Plant for Wear and Tear to be in addition to the cost of maintenance, chargeable to the Trading Account.

"A Renewals and Repairs Account, to equalise the charge to Trading Account.

"Inventory of Plant and Machinery.

"Accuracy of Balance Sheets.

"The illustrations given are few in number, but the principle suggested, if approved, may be applied in any variety of circumstances. The subject is an important one, and sufficient may have been said to create a desire to follow it out in more complete detail."

In a letter to the author, written some little time since, Mr. MURRAY said: "I do not know that there is anything in it (the above paper) which I would now alter, although I might add to it. I am more and more impressed with the importance of provision for renewals being placed upon a sound and systematic basis, having regard to the life of machinery, &c., and charging outlay against provision." In exemplification of his views Mr. MURRAY referred to the accounts of the Lancashire and Yorkshire Railway, in which—in addition to the actual cost of repairs—a fixed sum is charged to revenue for replacements, the actual expenditure upon replacements being charged against various "Renewals Funds," while the balance from time to time appears in the General Balance Sheet as a liability. It is believed that other railways adopt a similar system, but it is most unusual for the published accounts to actually show what has been done in the way of providing for future renewals.

DEPRECIATION TABLES.—It will have been noticed that, where a rate of depreciation upon machinery, &c., has been stated in the preceding paragraphs, it has usually been stated as being "upon the reducing balance": the advantage of this method is that the larger instalments are written off at first, when the machinery is new and its earning power greatest, but it is important to remember that the ultimate results attained by the two methods are widely different. Thus, if 5 per cent. per annum be written off £100 for twelve years the residual value will be £40, but if the same result is to be arrived at by calculating depreciation upon the reducing balances the rate to be employed must be $7\frac{1}{2}$ per cent. For the purpose of displaying similar comparative results under varying circum-

stances, the author has compiled a little work entitled *Comparative Depreciation Tables*, which, it is thought, will be found of value. A table on the "annuity" system for use in connection with freehold and leasehold properties is included in Appendix "D."

PROVISION FOR BAD AND DOUBTFUL DEBTS.

—Unless the outstanding Book Debts are extremely numerous, it is desirable that the Auditor should go over the list in company with his client, or the Managing Director, or some equally responsible authority, and settle the amount of loss to be provided for. Where the number of accounts renders this course impracticable, a certified list of amounts to be treated as bad, and a statement that the provision made is sufficient, signed by the aforesaid responsible authority should be supplied to the Auditor. In a lecture delivered to the Chartered Accountants Students' Society of London in 1898, Mr. DANIEL HILL, F.C.A., dissented from this view, holding that "although a client *ought* to know more about his customers than the Auditor does, an experienced Accountant will give a far more reliable valuation than the owner or Managing Director of a business can do." No doubt the training and experience of an Accountant helps him in many ways to gauge the probable realisable value of Book Debts; but unless his experience be confined to one particular industry (or at most to a few industries), his knowledge of the financial standing of the customers can of necessity be only fragmentary at the best. It is, moreover, thought to be undesirable for an Auditor to differ from the deliberate opinion of, say, a Managing Director, unless he is prepared to give solid reasons in support of his views. On the other hand, it is not intended to suggest that, merely because the Auditor has been supplied with a certified list of the provisions which it is thought necessary to make for Bad and Doubtful Debts, all he has to do is to accept it without further comment or inquiry. It, of course, remains for the Auditor to satisfy *himself* that the provision is one which appears to be both *bonâ fide* and reasonable. In this connection the following extract from an article which appeared

in *The Accountant* of the 12th January 1901 will be found useful:—

“With trading concerns debtors who always take a cash discount may, in the absence of information to the contrary, always be assumed to be good for any outstanding balance not greatly in excess of their ordinary amount. Debtors who always accept bills for their accounts may, under similar circumstances, be regarded as good, provided the bills are always met at maturity without renewal. Where there are renewals, the accounts should be examined more carefully; and, as the number of cases would not be large, this detailed inquiry would not be impracticable. Accounts showing an increasing debit balance require more careful scrutiny than those where the balance is reduced, more particularly if the number of transactions during the period be small. In the case of interest-bearing debts, the punctual payment of the interest may be taken as presumptive evidence that the principal is good, provided it be not in arrear; but where the interest is in arrear, the presumption is that the debt is at least doubtful, unless sufficient security is held to cover the amount. ‘Dead’ accounts are more likely to be doubtful or bad than ‘live’ accounts; and in this connection a debtor who, during the current year, has not paid enough cash to extinguish the balance against him at the commencement of the year, may generally be regarded as a ‘dead’ account, and treated accordingly. Apart from the open balances standing against the various debtors in the Customers’ Ledgers, it is important not to lose sight of unmatured acceptances, whether these be in hand or have been discounted; but, as has already been stated, a customer who invariably meets his bills at maturity may usually be regarded as safe to continue to do so.”

It may be added that, in many cases, there should be a fairly constant ratio between the amount of outstanding book debts and the total of the sales on credit during (say) the last three months.

Although it is very undesirable that an insufficient provision be made for bad debts, it should—on the other hand—be remembered that when once a debt is written off its chance of being eventually collected is greatly discounted; and, further, that there is at least the possibility of its not being accounted for, even if collected: hence the advisability of adopting the system already described (*vide* pages 58, and 59).

In connection with this subject, the judgments in the *Irish Woollen Co.* and the *National Bank of Wales* cases (*vide* Appendix "B") will be found of interest.

OUTSTANDING DISCOUNTS.—It is customary to provide for the usual cash discounts, upon both Book Debts and Trade Creditors, by means of a Suspense Account. Where, however, the amount is uncertain (by reason of the variable nature of the payments) and the difference between the two sides is but slight, the provision might be omitted without any great harm being done—indeed, it is a very open question whether the profit or loss—as the case may be—ought to be anticipated. *Trade* discounts are, however, a very different matter, and should always be provided for by deduction from the purchases and sales respectively.

It has been stated that every transaction on credit involves the consideration of interest or discount—a statement which is, doubtless, theoretically unassailable, but practically inconvenient. As a matter of fact, a result almost ideally correct may be obtained with a tithe of the trouble. If the terms upon which goods are sold are, say, $2\frac{1}{2}$ per cent. discount at one month, or a three months' acceptance net, it might, at first sight, appear that the trader gives credit at 15 per cent. per annum interest, but in all probability he would only allow 3 per cent. (or at most $3\frac{1}{2}$ per cent.) for cash, which is altogether a different rate. The real terms would thus be: 35 days' average credit (20th of month to 20th of month, payable 10th of following month), 3 per cent. or $3\frac{1}{2}$ per cent. discount; 65 days' average credit, $2\frac{1}{2}$ per cent. off; 126 days' average credit, net. It will be seen that these terms do not actually represent any definite rate of interest, and further—the choice of terms being with the debtor—that no absolutely accurate apportionment can be made.

In such a case as that named a better plan cannot be adopted than to suspend $2\frac{1}{2}$ per cent. on all open accounts, and carry over the Bills Receivable net. A similar method would apply

to outstanding liabilities and Bills Payable. Where, however, a Bill has been discounted or renewed at interest, or granted for an exceptionally long term at interest, the question of interest should be no longer ignored, unless the amount involved be trifling. The decision in *In re The Irish Woollen Co.* may be consulted with advantage here.

In the case of BANKS and other FINANCIAL HOUSES interest (which is no longer obscured by trade profits, but is itself the chief source of profit) must, of course, be *always* taken into account.

DIRECTORS' FEES.—In the absence of any special arrangement contained either in the articles of association or in the minutes of general meeting, Directors are entitled to no remuneration in respect of their services. The Auditor will require to see therefore, before passing any such remuneration, that provision is contained therefor in the articles of association, or else that the remuneration has been voted by the shareholders in general meeting. He would also require to see that the amount which the Directors have received is in accordance with such provisions. Proper vouchers should be given by Directors for fees received by them, and (unless specially so prescribed) the Income Tax payable upon such fees should—if paid by the company—be deducted from the sums payable to the individual Directors.

The case sometimes arises, in connection with companies which are not doing very well, of Directors foregoing the whole or a portion of their fees. In such a case as this it is desirable that the Auditor should inquire as to whether they have actually foregone the right to claim such fees, or merely foregone their immediate payment. In the latter case the amount still due should, of course, be included among the liabilities in the Balance Sheet. It is, perhaps, superfluous to add that no one who is not a Director can be entitled to receive Directors' Fees. As the Companies Act 1900 now requires every company to keep a Register of its Directors and Managers, it seems desirable

that this Register should be consulted when vouching the payments made, or due, to Directors in respect of fees.

PRELIMINARY EXPENSES.—In the Balance Sheet of almost every young company this item will be found among the Assets. It will probably surprise few to learn that, as the law is at present interpreted, registered companies are under no obligation to write off this item out of profits. It is, however, not only very desirable but also very usual to write off the amount of the Preliminary Expenses within the first three or five years; and the Auditor will do well to recommend the adoption of such a course. With Parliamentary Companies, on the other hand, Preliminary Expenses are an item of Capital Expenditure, and—as such—are retained upon the accounts for ever.

It must not be forgotten that, in every case, the Auditor must thoroughly verify the amount of this item by reference to vouchers and contracts. In particular, he should make sure that the company has made no payments that the promoters undertook to pay, or which—for other reasons—may appear improper. It is not an unknown occurrence for Directors' qualifications to be paid for out of Preliminary Expenses.

RESERVE FUND.—It is contended by some that a Reserve Fund *must* in all cases be invested in securities outside the business, but the view generally held by those competent to judge is that it is not—under ordinary circumstances—desirable that a Reserve Fund be specially invested if the moneys can be utilised to better advantage in the business itself, or in reducing its liabilities. Where, however, the fund is specially raised for a specific purpose (*e.g.*, the redemption of debentures) its investment would appear to be desirable, for the purpose of ensuring its being available at the appointed time. In certain other cases, as named in Appendix "A," Reserve Funds are required by statute to be specially invested; and in these cases it is, of course, the Auditor's duty to see that this has been done. Where the Reserve

Fund exists for the purpose of strengthening the credit of the company—as in the case of Banks—it is doubtless desirable that it should be invested in first-class securities; but it is no part of the Auditor's functions to interfere with the Management in this respect. The whole subject is, however, dealt with very fully in the following chapter.

Unless there is any special provision in the articles of association, there is nothing to prevent directors from transferring the whole or any portion of the amount standing to the credit of Reserve Fund to the credit of Profit and Loss Account, for the purpose of increasing the amount of profits available for dividends. Where such a course is being pursued, the Auditor should, however, take steps to acquaint the shareholders with the facts, unless they are sufficiently obvious on the face of the accounts.

? Prior to the passing of the Companies Act 1900 it was very generally thought that Premiums received upon the issue of shares ought in all cases to be credited to Reserve Fund; but it was not considered that this course was absolutely compulsory, while apparently there was nothing to prevent such Premiums being distributed as dividends by being transferred from Reserve Fund to the credit of Profit and Loss Appropriation Account. The Act of 1900, however, and the decision of the Court of Appeal in the case of *Burrows v. Matabele Gold Reefs and Estates Co., Lim.*, raised a doubt as to whether Premiums must not be treated as a receipt on account of Capital rather than on account of Revenue. The House of Lords has, however, in *Hilder v. Dexter* (*vide* Appendix "B"), overruled the Court of Appeal in the case already referred to, and the position would thus appear to be the same as it was before the 1900 Act. That is to say, although it is obviously desirable that Premiums received on the issue of shares and debentures should be placed to the credit of a permanent Reserve Fund, and not applied to the equalisation of dividends, there is apparently nothing in the Companies Acts

to prevent their being divided, either at once or at any subsequent date. The Court of Appeal has decided, *In re Hoare & Co., Lim.* (*vide* Appendix "B"), that a Reserve Fund originally constituted out of premiums received on the issue of shares need not be exhausted before a scheme for the reduction of capital can be entertained.

INSPECTION OF MINUTE BOOK.—The question frequently arises, and is the source of no little contention, as to whether an Auditor has the right to inspect the Minute Book recording the proceedings at board meetings. It is thought, however, that this right cannot be disputed, inasmuch as it is clearly the duty of the Auditor to certify to the accounts after having examined "the books of the company"; and certainly the Minute Book is a "book of the company," inasmuch as it is one of the few books which every company is required by Act of Parliament to keep. Theoretically, at least, it is necessary that the Auditor should carefully examine the whole contents of the Minute Book, but in practice it is thought that this rule may frequently be relaxed, and reference only made in respect of items upon which the Auditor is in doubt, or with regard to which he requires further elucidation. It need hardly be added, however, that in this respect—as with regard to all other matters where the Auditor prefers to take a short cut in his work—he does so at his own risk, and the risk in this particular connection is that he may fail to become acquainted with some contingent liability or contract which would materially alter his views with reference to the accounts which he is called upon to certify.

It is thought that the Companies Act 1900 supports the views expressed in the previous paragraph (which appeared in all the earlier editions of this work), and it may be noted that the opinion of Counsel—which is referred to in a later chapter—expressly endorses this view. If an Auditor is refused facilities for performing his duties, whether such refusal takes the form of declining to allow him access to any of the "books, accounts, or vouchers of the company," or to the failure of the

directors or officers of the company to give such information or explanation as may be necessary, the Auditor should sign a certificate at the foot of the Balance Sheet stating that all his requirements as Auditor have not been complied with.

REDEEMABLE DEBENTURES.—Where debentures, redeemable at par or at a premium, have been issued at a lower rate, it is essential that a proper reserve be made to meet the deficit; and it will be the Auditor's duty to see that a sufficient provision is made.

FORFEITED SHARES, not reissued, should be separately stated on the Balance Sheet, as a dividend declared would not be payable in respect thereof. Such shares may at any subsequent date be reissued at any discount not exceeding the amount per share already received, and when so reissued the amount already paid (or so much thereof as represents profit) should be treated as a premium upon issue, and credited to Reserve Fund. The Auditor should always make a point of seeing that the minutes as to forfeiture and as to the calls due are *prima facie* in order.

SECRET RESERVES.—This most debatable subject is approached with considerable diffidence. Very much can be (and has been) said upon both sides of the question, making it a most difficult thing to say what is really the correct course to adopt in any particular case; and, if the question be complicated, even when a particular instance is judged upon its own merits, how much more difficult is it to lay down any general rules of universal application.

The object of all secret reserves is to equalise dividends, or to equalise apparent profits; and, in the case of banks and similar institutions, it must be admitted that, were accounts published showing considerable fluctuations in the amount of profits earned, the result might readily be to produce a feeling of disquietude which was altogether unwarranted by the actual facts. More particularly in the case of banks largely affected by fluctuations in exchange does it seem desirable that the temporary

effect of such fluctuations should be excluded from published accounts. The understating of assets in profitable years (which is the ordinary means of providing a secret reserve) clearly contemplates, however, the possibility of their being written up in less profitable years, when it may be desired not to disclose the fact that the profit earned has been less than usual, or perhaps even insufficient to cover the proposed dividend.

Opinions differ greatly as to the extent to which the formation of secret reserves is permissible; but it is thought that, within reasonable limits, the matter is one resting with the Directors rather than with the Auditor, so long as there is no suspicion of bad faith. It is when it is sought to have recourse to a secret reserve by writing up those assets which have hitherto been undervalued that the position requires the most serious consideration of the Auditor, and upon this point a few precedents may prove of interest.

Some time since the accounts of the London General Omnibus Company, Lim., were criticised, because the Balance Sheet contained upon the assets' side an item of considerable magnitude described as "Times," representing, apparently, the assumed value of the Goodwill attaching to the times of the company's omnibuses. In order to meet this criticism the item "Times" was eliminated, and the value of the company's leasehold premises written up to a corresponding extent, it being stated that—even at this enhanced valuation—the leaseholds appeared at a figure lower than their intrinsic value. The matter was not made the subject of legal proceedings; but, in view of the attention which it attracted, it may, it is thought, be safely assumed that it was found impossible to attack this policy upon legal grounds.

A more important precedent is the case of *Bolton v. The Natal Land & Colonisation Company, Lim.* (*vide* Appendix "B"), in which it was held that the company might properly declare a dividend out of current profits under the following circumstances:—A large bad debt had been made in previous

years, and the loss so shown upon the accounts was cancelled by writing up the value of the company's lands to a corresponding extent. It may be mentioned, however, that in the case of a land company, its lands—which are held for purposes of re-sale—are floating assets, and it was expressly stated by Lord (then Mr.) Justice ROMER, in the course of his judgment, that it was “not correct, in estimating the profits of a year, to take into account the increase or decrease in the value of the capital assets of the company.”

With regard to the position of the Auditor generally it would appear that, in the absence of *mala fides*, he incurs but little responsibility. He should, however, be very careful about the good faith with which the valuations or re-valuations are made, and although he has no power to influence the management in the exercise of their *bonâ fide* discretion, yet it would appear to be clearly his duty, in cases of doubt, to sufficiently acquaint the shareholders with the facts of the case to enable them to intelligently exercise their own discretion as to whether they will pass the accounts in the form in which they are presented to them or not. Thus, where the assets are stated below their certainly-known value (forming a secret reserve), or above their certainly-known value (forming a secret deficit), at least the bare fact should be mentioned in the Auditor's report. Again, there are limits to the extent with which a secret reserve should be played with, for the sake of equalising dividends; and it is very undesirable that valuable assets should be omitted from the Balance Sheet *in toto*, because in such a case the Auditor is very liable to omit to verify their existence. In some Balance Sheets a note is appended to the effect that certain (specified) assets have not been included. Such a course appears to remove the most weighty objections that can be raised against the reduction of valuable assets to zero.

It has not been thought desirable to alter the foregoing paragraphs, which appeared in the sixth edition of this work; the decision of Lord (then Mr.) Justice BUCKLEY in *Newton v. Birmingham Small Arms Company, Lim.* (*vide* Appendix “B”),

has, however, since been given, and throws much additional light upon the subject. In the first place it shows that secret reserves are sometimes represented by outside investments that are not disclosed at all upon the face of the Balance Sheet (reserves that can only be created by, in effect, debiting Revenue with a payment that in no sense represents an expense); secondly, it shows that a company may, by its articles of association, deprive its members of their natural right to a "full and fair" Balance Sheet; thirdly, that an Auditor is not *bound* to disclose the fact that the financial position of the company is better than the position shown by the Balance Sheet issued by the company; fourthly, that neither memorandum nor articles of association can take from the Auditor his statutory right of reporting to the shareholders on the (whole) accounts of the company, and that provisions purporting to do so are void *ipso facto*. Those desirous of entirely withholding the secret reserve from the cognisance of the Auditor might attain their end by authorising the directors for the time being to make payments in their absolute discretion to third parties, who might agree to act as informal trustees of the moneys so handed over, provided the necessary powers were contained in the memorandum of association; but no articles could authorise such a disposition of the company's revenue earnings.

Undoubtedly the usual object of a secret reserve is to impart a fictitious appearance of stability to the profits of a prosperous but fluctuating business: this, in itself, seems to be entirely legitimate. Sometimes, however, the object—or one object—is to secure the command of moneys that may be expended without being accounted for. Thus a secret reserve might conceivably be employed (1) in securing control of allied undertakings upon the American Trust principle, in which case the value of the "investment" may be quite speculative; (2) in investments in, or loans to, undertakings in which the directors are personally interested, in which case the application may not be at all in the interests of the

company; (3) in commissions or bribes to the agents of customers and others, *i.e.*, in ways declared criminal by the Prevention of Corruption Act 1906; (4) in voting "additional remuneration" to the directors or their friends.

It is clear from the decision in the *Birmingham Small Arms* case that the duty is cast upon the Auditor of reporting to the shareholders in all cases where he considers that the assets representing the secret reserve have been misapplied: his position in this respect is thus one of the gravest responsibility.

FOREIGN EXCHANGES.—The treatment of foreign exchanges in books of account appertains to bookkeeping rather than auditing, and the subject will accordingly be found to be fully dealt with in the author's *Advanced Accounting*. From the point of view of the Auditor all that is necessary is that the accounts should properly disclose the true position of affairs. For this purpose it is only necessary to bear in mind that the Trial Balance (from which the accounts are compiled) is a summary of *transactions* that have actually taken place, temporarily recorded, for the sake of convenience, in the medium of a foreign currency. To determine their proper valuation in sterling it is necessary that the nature of these various records should be inquired into; that the Revenue Account (whatever its precise form) should correctly show, under suitable headings, the totals of the various kinds of transactions on account of Revenue, and that the Balance Sheet should fairly state the Assets and Liabilities—those of a floating nature at their realisable cash value, while the fixed or permanent items may be maintained at the original amount, subject only to such provision for Depreciation as may be necessary in view of their wasting character. If this position of affairs be correctly comprehended, there is no more difficulty in auditing accounts figured in a foreign currency than in auditing accounts the narration to which is expressed in a foreign language. The medium of expression in neither case affects the nature of the facts.

ULTRA VIRES.—It is a question of some nicety as to how far an Auditor is expected to concern himself with the validity of the transactions that come under his notice. It may be taken that, in general, the Auditor is not constituted a judge of the conduct of the directors in their administrative capacity ; and that, so long as the accounts are in order, and in accordance with such statutory provisions as may affect the particular undertaking, and its memorandum or articles of association (or their equivalent), the Auditor need not concern himself with questions which his professional training has not especially qualified him to solve. It is clear, however, that when the Auditor is aware that irregularities have been committed, it becomes his duty to report the whole circumstances to the shareholders (*c.f.* decision in the *Birmingham Small Arms* case referred to on page 246).

It is perhaps worth noting that such registered companies as are regulated by Table "A" of the 1862 Act have no power to declare interim dividends, although in practice interim dividends are frequently declared. They are clearly irregular, however, and the Auditor should therefore refer to the matter in his report. The "new" Table "A" (1906) authorises the payment of interim dividends.

CHAPTER VII.

FORM OF ACCOUNTS AND BALANCE SHEETS.

It has already been very clearly stated that, in general, the Auditor is not responsible for the form of the accounts which he certifies. The consideration of the form that such accounts should properly take is, therefore, not strictly a matter within the scope of the present work. Still, it is none the less true that, as a matter of fact, Auditors are frequently asked to settle questions of form; and although in the case of limited companies' accounts they will often be only prudent if they decline to accept a responsibility that properly devolves upon the directors, there can, it is thought, be no possible objection in the case of the accounts of private firms. Moreover, it cannot be denied that the subject is at all times one upon which the Auditor should have definite and well-matured opinions.

It may be stated at the outset that the accounts which it is now proposed to deal with are those which are ordinarily published as "the audited accounts"—viz., the Revenue Account (or its equivalents) and the Balance Sheet.

OBJECT OF REVENUE ACCOUNTS.—Taking first the account which in different undertakings is variously called the Trading Account, the Manufacturing Account, the Working Account, the Profit and Loss Account, and the Revenue Account, the first point to be considered is the real object of

preparing such an account. This may be stated to be for the purpose of showing—

First, the amount of business done in each of the various branches in which business is carried on;

Secondly, the amount of expenditure in each of the branches, or departments, necessary for the carrying on of that business; and

Thirdly, the amount of surplus, or profit—or loss, as the case may be—which arises from the carrying on of the business.

The object of the information is doubtless primarily to ascertain the amount of ultimate profit or loss, but beyond this there is also the further object—which, perhaps, is only fully appreciated by those skilled in accounts—of comparing the corresponding items of various periods, with a view to ascertain how income may be increased and expenditure reduced, or, on the other hand (so far as possible), *why* income has become reduced, and *why* expenditure has increased.

It will thus be seen that the efficiency of this account depends very materially upon the skill with which the income and expenditure have been distributed over the various headings employed, and consequently it becomes necessary to discuss the nature of the various headings under which the items of this account should be divided.

It goes without saying that, inasmuch as this account details the summarised result of the transactions recorded in the books, its exact nature will very materially depend upon the precise business which is being carried on. It therefore becomes necessary to further consider the subject under the headings of various classes of business.

COMMERCIAL ACCOUNTS.—Taking first commercial concerns (which undoubtedly represent the great majority of the undertakings which are now being considered), it will be found

that the transactions consist in the buying of goods and the selling thereof, either in the precise form in which they were purchased (as in the case of traders), or in an altered form (as in the case of manufacturers); in both cases there being the further expenditure incidental to the carrying on of the undertaking.

ACCOUNTS OF TRADERS.—Dealing first with the Accounts of Traders, which are naturally of a simpler nature than those which require to be kept by manufacturers, the first circumstance to note is the method usually in vogue by which a trader computes the amount of advance upon purchase price which it is necessary for him to charge for his goods in order to obtain a remunerative return for his labour, and this excess is very generally known by the term of "Gross Profit." It would be very difficult to find an exact definition of the term "Gross Profit," inasmuch as the items from which it is calculated will be found to vary in different undertakings; but seeing that the whole business of a trader is based upon the calculation of a fixed percentage of gross profit upon each different class of goods dealt with, it necessarily follows that any form of accounts which does not recognise the existence of such a thing as "Gross Profit" fails to afford the trader that assistance which he is entitled to look for from his accounts, and consequently to a very great extent fails to justify its existence.

It has been argued by many experienced accountants that Gross Profit cannot be considered to arise until such things as rent of warehouse, salaries of warehousemen, &c., have been debited to the Trading Account; but as it is the almost universal custom of traders to reckon their percentage of gross profit entirely from the cost price of their *goods* (although, as a matter of convenience, they actually make the calculation backwards from their selling price) it would seem that, however correct it may be in theory, it is in practice nothing more than pedantic to include in this first section of the account anything more than "Sales" and the closing "Stock" upon the credit side, and "Purchases" and the opening "Stock" upon the debit. It is, of course, quite possible to argue that the resultant

credit balance means absolutely nothing at all; but, even if this were so, the fact remains that unless the account be so prepared it is impossible to see whether the aggregate transactions of a period actually result in the percentage of gross profit which the trader had been calculating upon throughout that period; and, therefore, whether it is thought best to call the balance of this first section "Gross Profit," or to employ the indefinite term "Balance," the overwhelming weight of advantage lies in bringing the account—in this respect at least—into accord with the custom of every trader, and so enabling him to ascertain whether during any period he has actually achieved the results which he anticipated.

In the second section of the Revenue Account may be included all items of income and expenditure relating to the business. These expenses should be grouped in convenient sub-sections, so that the effect of each group upon the whole may be readily perceived. This is useful both for the purpose of seeing how far the net profits of a concern have been affected by purely financial reasons, and how far by commercial reasons, and also on account of the convenience it affords if it should at any future time be decided to convert the venture into a limited liability company.

The following *pro formâ* accounts are drawn up upon these lines, and represent a good form for a firm of traders:—

Dr. TRADING ACCOUNT (FIRST SECTION) FOR THE YEAR ENDED 31ST DECEMBER 1906. Cr.

	Stock on 1st Jan 1906		Purchases for the year		Gross Profit		Total		Sales for the year		Stock on 31st Dec. 1906		Total	
	£	s d	£	s d	£	s d	£	s d	£	s d	£	s d	£	s d
Grocery Department..	20,000	0 0	13,500	0 0	1,500	0 0	35,000	0 0	10,000	0 0	25,000	0 0	35,000	0 0
Wines and Spirits Department ..	7,500	0 0	34,500	0 0	4,000	0 0	46,000	0 0	40,000	0 0	6,000	0 0	46,000	0 0
Drapery Department ..	4,750	0 0	4,625	0 0	625	0 0	10,000	0 0	5,000	0 0	5,000	0 0	10,000	0 0
Tailoring " ..	5,000	0 0	10,375	0 0	2,625	0 0	18,000	0 0	15,000	0 0	3,000	0 0	18,000	0 0
Mantle " ..	3,500	0 0	3,025	0 0	875	0 0	8,000	0 0	5,000	0 0	3,000	0 0	8,000	0 0
Fancy Goods " ..	12,000	0 0	26,500	0 0	2,500	0 0	41,000	0 0	25,000	0 0	16,000	0 0	41,000	0 0
Furniture " ..	£55,000	0 0	£110,875	0 0	£14,125	0 0	£180,000	0 0	£120,000	0 0	£60,000	0 0	£180,000	0 0

Dr. PROFIT AND LOSS ACCOUNT (SECOND SECTION) FOR THE YEAR ENDED 31ST DECEMBER 1906. Cr.

	£		s d		By Gross Profit for the year, as per Trading Account ..	£	s d	£	s d
	£	s d	£	s d					
To Rent, Rates, and Taxes ..	..	..	..	..	..	..	..	..	..
" Salaries of Assistants, &c., viz. :-	..	..	..	..	..	..	..	..	..
Salaries ..	..	£4,000	0 0	..	..	..	..	..	..
Cost of Board ..	..	..	£2,500	0 0	..	..	..	..	..
Trade Expenses ..	..	..	..	..	..	6,500	0 0	..	..
" Carriage ..	..	..	..	..	..	1,500	0 3	..	..
" Depreciation ..	..	..	..	..	..	1,000	0 0	..	..
" Interest on Capital ..	..	..	..	..	..	250	0 0	..	..
" Income Tax ..	..	..	..	..	..	2,500	0 0	11,250	0 0
" Balance being Net Profit for the Year, viz. :-	..	..	..	..	..	125	0 0	2,625	0 0
A., one-half share ..	..	..	..	..	..	1,287	10 0	..	..
B., one-third share ..	..	..	..	..	..	858	6 8	..	..
C., one-sixth share ..	..	..	..	..	..	429	3 4	..	..
	..	..	..	..	..	..	..	2,575	0 0
	..	..	..	..	..	..	..	£16,450	0 0

* Discounts upon Sales (if any) should be shown separately, on the debit side of this account.

MANUFACTURERS' ACCOUNTS.—Passing on to the accounts of manufacturers, it is first necessary to subdivide this heading in accordance with the various classes of business that fall hereunder. There is first of all the class of manufacturers but slightly removed from the trader—that is to say, the manufacturer who does not require to sink a large proportion of his capital in expensive plant and machinery, the most typical examples of which are, perhaps, that of the small manufacturing jeweller and the small manufacturing tailor—both of whom, by the way, are fast dying out. In this class, as with traders pure and simple, the selling price is based upon a percentage of so-called “Gross Profit,” the outlay in this case being the cost of materials together with the wages spent upon manufacturing; and, therefore, although the method is clearly indefensible from a theoretical point of view, the division between the first and second sections may conveniently be drawn exactly where it is drawn by the manufacturer himself in his mental calculations. Those who wish to have their accounts as complete as possible may prefer in addition to make a further subdivision of this account in the second section, separating the expenses of manufacturing (such as rent of factory, wages paid for supervision of workers, depreciation of plant, &c.) from those expenses which relate more particularly to the storing of goods and the selling thereof; but inasmuch as the balance shown by this break would correspond with nothing in the mind of the manufacturer it appears to be superfluous, and it will probably be thought sufficient to merely show separate totals for these classes of expenditure in the same section, as shown below:—

Dr: TRADING ACCOUNT (FIRST SECTION) FOR THE YEAR ENDED 31ST DECEMBER 1906. Cr:

[illegible]

Dr. PROFIT AND LOSS ACCOUNT (SECOND SECTION) FOR THE YEAR ENDED 31ST DECEMBER 1906. Cr.

	£	s	d
To Factory Expenses, viz. :—			
Rent, Rates, Taxes, &c.	100	0	0
Salaries	250	0	0
Depreciation	50	0	0
General Expenses	100	0	0
Warehouse Expenses, viz. :—	500	0	0
Rent, Rates, Taxes, &c.	200	0	0
Salaries	400	0	0
Depreciation	50	0	0
General Expenses	250	0	0
Interest upon Capital	500	0	0
" Discount upon Sales	300	0	0
" Income Tax	62	10	0
Balance, being Net Profit for the year, viz. :—	862	10	0
A., three-fifths share	1,462	10	0
B., two-fifths share	975	0	0
	2,437	10	0
	£4,700	0	0

The manufacturers belonging to the next class are those whose transactions consist in the manufacture of one or more classes of goods involving expensive plant, which goods are first manufactured and then warehoused before being sold. These undertakings are naturally upon a much larger scale than those which have just been considered, and consequently it will be found that the accounts are, as a rule, more scientifically kept, and the method of costing more complete.

The first section of the account thus becomes divided into two parts, upon what may be called parallel lines, viz.:—

The Manufacturing Account, which deals with the conversion of raw material into manufactured articles, and shows the profit upon manufacture and the stock of raw materials on hand.

The Trading Account proper, drawn upon the same lines as the first section of a trader's Profit and Loss Account.

The second section of the account does not present any new features that call for consideration.

The form shown below is thought to be the most suitable one for this class of accounts, but, of course, the precise wording will depend entirely upon the particular industry carried on. The expenses included in the Manufacturing Account will (as a rule) be those which are dealt with in the Cost Accounts, and those only. It is quite likely, therefore, that Factory expenses would be debited to the Manufacturing Account, rather than to the Profit and Loss Account, although the effect of so doing would be to obscure the percentage of (so-called) gross profit.

The figures shown are the same figures as those employed in the first section of the account stated above, re-drafted for the purpose of separating the results of manufacturing from those of trading.

CONTRACTORS' ACCOUNTS.—The next class of manufacturers to be dealt with consists of those that may conveniently be summarised under the head of "Contractors," *i.e.*, those manufacturers who only make articles which have already been sold for an agreed price. To this class belong builders and many engineers.

It is, perhaps, more in this class than anywhere else that the absolute necessity of proper Cost Accounts is so evident. Indeed, all contractors' accounts may be regarded as incomplete which do not provide, in addition to an ordinary Profit and Loss Account, a "Summary of Cost Account," showing the same result. This being done, the chief interest centres round the Cost Account rather than the Profit and Loss Account itself, and there is thus less necessity for the latter to be unduly elaborate. It is therefore usually best to state this latter account in one section only, as shown below.

The Summary of Cost Account may be shown in a tabulated form, the totals of the vertical columns agreeing with the various items of the Profit and Loss Account (but, perhaps, somewhat more summarised in form), while the details of the columns headed "Profit and Loss" would show the actual amount of profit realised or loss incurred over the execution of each separate contract, thus:—

SUMMARY OF COST ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER 1906.																		Cr.	
Number of Contract	Forward from last Account	Wages		Stores Issued	Materials Purchased	Plant Issued	Special Expenses	General Expenses	Discount and Interest	Net Profit on Contract	Total	Number of Contract	Amount of Contract	Stores Returned or Sold	Plant or Sold	Total Loss on Contract	Total Cost of Contract (if uncompleted) carried forward	Total	
		Hours of Time*	Amount																
1,285	10,000	10	£ 400	£ 500	£ 250	£ ..	£ 10	£ 62	£ 9	£ 650	£ 11,881	1,285	£ 10,000	81	£ 1,800	£ ..	£ ..	£ 11,881	
1,286	5,000	50	£ 2,000	£ 1,500	£ 4,750	£ 750	£ 40	£ 312	£ 42	£ ..	£ 14,394	1,286	£ 12,500	194	£ 700	£ 1,000	£ ..	£ 14,394	
1,287	..	100	£ 4,100	£ 2,500	£ 7,500	£ 1,250	£ 120	£ 625	£ 83	£ 950	£ 17,128	1,287	£ 16,000	28	£ 1,000	£ ..	£ ..	£ 17,128	
&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	&c.	
£20,000†	£20,000	1,200	£50,000	£46,000	£72,000	£25,000	£2,500	£7,500	£1,000	£27,500	£251,500	£200,000	£200,000	£6,000	£22,500	£1,000	£22,000‡	£251,500	
																		* Omitting "000's"	
																		† Sundry Debtors	
																		Stores ..	£16,000
																		Plant ..	2,000
																		Plant ..	2,000
																		£20,000	
																		‡ Sundry Debtors	
																		Stores ..	£15,000
																		Plant ..	4,500
																		Plant ..	2,500
																		£22,000	

It is, perhaps, unnecessary to add that, in practice, an absolute agreement between the Profit and Loss Account and the Summary of Cost Account is hardly to be expected; but a very close approximation must be arrived at before either can be safely relied upon.

STATISTICAL INFORMATION.—In connection with all the preceding accounts it will usually be found of the very greatest assistance to add statistical columns, for the purpose of showing the relation which each item bears to the amount of trade done. This relation will usually be expressed in the form of a percentage on the amount of the sales, but where the business deals with articles of a uniform or similar character—as, for instance, in the case of collieries, brickyards, and the like—the percentage will probably be based upon some quantity, or unit, of the goods dealt in, as “per ton of coal” or “per thousand bricks,” and in these cases it is usually thought more convenient for the unit to be the production rather than the sale. This view is confirmed by an interesting lecture on “The Form of Revenue Accounts and Balance Sheets, and the use of percentages in connection therewith,” by Mr. RICHARD BROWN, C.A., reproduced in *The Accountants’ Magazine*, March 1904.

In published accounts it is also somewhat usual, and very convenient, to publish, side by side with the figures for the current period, those for the next preceding period, for the purposes of comparison. For the sake of clearness these are best placed on the left-hand side of the description of the various items, and in italics, or some other type which may be readily distinguished from that in which the accounts for the current year are printed.

MINING ACCOUNTS.—Another very important class of accounts, which can hardly be said to come under any of the previous headings, are those relating to Mines. These accounts are best dealt with in two sections: one to include all the items relating to the actual working of the undertaking; and the other, those appertaining more particularly to finance. Cost Accounts would be made weekly or monthly, but they would usually form no part of the annual accounts.

“NET PROFIT.”—This is, perhaps, the proper place to offer a protest against the method adopted by many companies

of stating in their published accounts a so-called "Net Profit," *out of* which it is proposed to set aside a certain sum for Depreciation and Directors' Fees. A true net profit can only be arrived at after charging up *all* expenses—including, of course, Depreciation, Directors' Fees, Interest on Debentures, &c. &c.

STATUTORY FORMS OF ACCOUNT.—The foregoing remarks as to forms of account do not, of course, relate to those undertakings whose accounts are specially provided for by Act of Parliament. These are:—

The accounts of such Railways and Tramways as come under the provisions of the Regulation of Railways Act 1868.

The accounts of such Gas Companies as come under the provisions of the Gas Works Clauses Act 1871.

The accounts of Life Assurance Companies, which come under the provisions of the Life Assurance Companies Act 1870.

The accounts of Electric Lighting undertakings, which come under the provisions of the Electric Lighting Clauses Act 1899.

And a few other undertakings (such as Building and Friendly Societies), to which many of the points now being raised do not apply, or apply only in modified form.

Inasmuch, however, as the form of accounts provided in each of these cases is probably as excellent a one as could well be conceived (due exception being always taken to the transposed form of Revenue Account provided for Life Assurance Offices), it is clearly advisable to adopt it whenever appropriate, even in such cases as it is not absolutely compulsory, and this also applies (to a certain extent, at all events) to the accounts of Water Companies, which possess many features in common with those of Gas Companies, although, strangely enough, there is no statutory form for the accounts of such undertakings.

BALANCE SHEETS.—Turning now to the question of Balance Sheets, perhaps the first point to be disposed of is the rival advantages of the Single and Double Account Systems.

SINGLE AND DOUBLE ACCOUNT SYSTEMS.—In undertakings whose accounts are based upon the latter system it is assumed that the capital of the undertaking has been sunk in the purchase and construction of definite permanent works, and the Balance Sheet is divided into two portions, one showing, on the one hand, the expenditure on such works, and upon the other the capital raised wherewith to meet such expenditure, while the second section, or “General Balance Sheet,” contains what may be conveniently called the “floating” assets and liabilities arising incidentally in the course of carrying on the undertaking. It has been thought by some that this method of stating the accounts absolved the company from making any provision to meet depreciation of its permanent assets, and to a certain extent (*e.g.*, with regard to preliminary expenses) this would appear to have been the intention of the Legislature; but what was really intended seems to have been that Fluctuation, rather than Depreciation, was to be disregarded; and it is, perhaps, well to call attention to the fact that it is not only possible but also perfectly easy for provision for Depreciation to be made and stated in accounts kept upon the Double Account System. In point of fact provision *must* be made for the depreciation of wasting assets that call for renewal—the only open question is *when* the provision shall be made.

WHAT ARE ASSETS?—Going back to first principles, it must be admitted that an asset may be fairly defined as “an expenditure upon a remunerative object,” and, indeed, it may be taken as the test of whether any particular expenditure is an asset or a loss to inquire whether as a matter of fact such expenditure is—looking back at it—worth the amount expended upon it. This applies whether the expenditure is in the nature of capital spent in the purchase or construction of any particular property, or in the purchase of property or

labour which was subsequently sold to another. In the former case, if—looking back upon it—it is considered that if the opportunity of making the investment a second time should again arise it might reasonably be made upon the same terms, it may fairly be said that there is value for the original outlay ; and in the latter case, if—looking back upon it in the light of present experience—one would again sell upon trust to any particular individual property upon which time or money had been expended, it may fairly be said that value is still remaining for the amount with which it at present stands charged. If, on the other hand, it appears that the value remaining for such expenditure is less than the original amount of such expenditure, it is obvious that, as a matter of fact, Depreciation (or loss) has occurred.

NECESSITY FOR DEPRECIATION.—With regard to those few classes of undertakings whose accounts the law requires to be kept upon the Double Account System, it would appear that (in view of the permanence of the undertaking and the subsequent remoteness of realisation and an *ascertained* loss) the Legislature does not require any provision to be made to meet such Depreciation, except in the case of leaseholds ; but it requires all expenditure upon maintenance and renewals to be borne by Revenue, and it indirectly sanctions (where it does not expressly enforce) the provision of a prudent Reserve to meet any outlay that may in future be required to keep the property in a state of working efficiency equal to that in which it at first stood. On the other hand, it is a very generally accepted principle with regard to those undertakings which are not specially provided for by the Legislature, that before reckoning profits an adequate sum should be set aside to meet any loss arising from the Depreciation of property ; curiously enough, however, it would appear doubtful as to whether the law *compels* any such company to make provision for Depreciation before declaring dividends out of its earnings.

In both cases, therefore, the question of Depreciation is rather one of prudence, or of internal administration, than of

legal compulsion; and, moreover, it will be seen that there is no essential difference in this respect between accounts kept upon the Single Account System and those kept upon the Double Account System. In both cases Depreciation must, of course, regularly take place, and it is usual to provide for it, although the method employed under the two systems naturally varies.

METHOD OF PROVIDING FOR DEPRECIATION.—

With the Double Account System, it being undesirable to deduct the Depreciation from the original cost shown in the Capital Expenditure Account, the method adopted is to accumulate the amount set aside from time to time upon a Depreciation (Fund) Account, or a Reserve for Repairs and Renewals Account, which is included as a liability in the General Balance Sheet (although not necessarily stated separately). On the other hand, the more usual course to adopt with accounts kept upon the Single Account System is to deduct the amount written off for Depreciation from the amount at which the value of the asset is stated, and this whether the Assets Account and Depreciation Account are kept separate in the Ledger or not.

It may be mentioned, however, that although theoretically the distinction between the Double Account System and the Single Account System is that described above, it is not invariably adhered to in practice. Under the Single Account System, Reserves to cover Depreciation, &c., are not infrequently shown upon the liabilities' side of the Balance Sheet, instead of being deducted from their respective assets; while the Chelsea Electricity Supply Company, Lim., has issued accounts (prepared upon the Double Account System) showing a considerable sum written off Capital Expenditure under each of the various headings: a plan which has also been recommended by the Municipal Tramways Association. It may be pointed out, however, that a Reserve for Depreciation is *not* a Reserve Fund, and should not be so styled.

CHOICE BETWEEN DOUBLE AND SINGLE ACCOUNT SYSTEMS.—It will therefore be seen that the question as to whether a certain set of accounts should be kept upon the Double or the Single Account System, however interesting it may be in other respects, does not really in the least affect the question of the desirability or necessity of making an adequate provision for the Depreciation of wasting assets. There is this, however, to be said—that while, with accounts stated upon the Double Account System, it will naturally be assumed (in the absence of evidence to the contrary) that no such provision has been made in excess of the actual expenditure upon renewals to date (if any), it will in the case of accounts kept upon the Single Account System be as naturally supposed that the values assigned to the various assets are actual, and not fictitious, amounts. Consequently in those undertakings where it is difficult, if not impossible, to assign an accurate value to a company's assets (and where those assets are of a permanent nature and represent the bulk of the working capital), the Double Account System may advantageously be adopted, as being the less likely to create a misapprehension upon the part of the shareholders. For example, in the case of a single-ship company it is usual to make no allowance for Depreciation of the value of the vessel, which naturally represents practically the whole of the company's capital. Such a case is particularly suitable for the Double Account System, and that for the simple reason that this system best records the actual facts of the case.

On the other hand, with companies who venture the bulk of their capital in any ordinary trade, the question is widely different; for in such cases the permanent assets naturally form a much smaller proportion of the total capital, and consequently the Double Account System (which pre-supposes the investment of practically the whole capital of the undertaking in permanent assets with which the business of the company is carried on) does not apply. In these cases, therefore, it is essential that all assets which are not taken into account at what may fairly be assumed to be their value at the date of the accounts should be definitely stated to be "at cost."

The various items which are ordinarily found upon a Balance Sheet will now be dealt with in order, and the best form of wording under various circumstances considered. For this purpose the best course will be to take as a model the form of Balance Sheet provided in "Table A" of the Companies Act 1862, which sets the liabilities upon the left-hand side and the assets upon the right-hand side, commencing upon both sides with the most permanent items and leaving those which are most constantly varying to the last.

FORM OF BALANCE SHEET.—Some years ago it was not unusual to find Balance Sheets stated with the assets upon the left-hand and the liabilities upon the right-hand side. The circumstance is, doubtless, at first sight curious, but, like many other things, there was good reason underlying this apparent anomaly. Under the Italian system of bookkeeping, which is still practised in some old-fashioned merchants' houses, it is the custom at every period of balancing, after the Nominal Accounts have been closed, to transfer the balances of the Real and Personal Accounts into one account, usually called in England the "Balance Account," and in France the "*Balance de Sortir*," or "Closing Balance." Under such circumstances, the Ledger would be actually closed (which, in fact, is never the case under the ordinary English system), and the Balance Account so raised would practically be a detailed Balance Sheet, but with the assets upon the *Dr.* and the liabilities upon the *Cr.* side, as shown in the old-fashioned Balance Sheets already referred to. The re-opening of the Ledger for the next period's transactions would necessitate the *writing back* of the balances of the Real and Personal Accounts to their respective headings; which would involve (for the sake of completing the Double Entry) a second Balance Sheet ("*Balance d'Ouvert*"), but with the sides transposed, viz., the liabilities upon the *Dr.* and the assets upon the *Cr.* side. Why this latter, rather than the former, should be the form which is now generally adopted it is not very easy to see; but, perhaps, the best reason that can be given is that insomuch as a set of books must be formally

opened before it can be closed, the first Balance Sheet will naturally be in the form of an Opening Balance Sheet in the modern form; and that, consequently, where the abbreviated methods of modern bookkeeping dispensed with the actual closing of the books at each balancing, it would be natural to adhere to the form of Balance Sheet which was used in the first instance. Inasmuch, however, as the modern Balance Sheet is not a Ledger Account, but merely a summarised extract from the Ledger, many accountants consider that the headings "*Dr.*" and "*Cr.*," "*To*" and "*By*," are out of date, and do not, therefore, employ them in Balance Sheets. It has been argued in some quarters that the Balance Sheet is a Ledger Account, and that therefore these signs ought not to be omitted. The matter is, of course, of no real importance either one way or the other; but when the statement that the Balance Sheet must of necessity be a Ledger Account has to be supported by such explanations as the following, it may well be questioned whether the artificiality of the argument does not help to disprove the original proposition. In a lecture delivered at a meeting of the Chartered Accountants Students' Society, of London, in 1894, Mr. ERNEST COOPER, F.C.A., said, "In the Ledger the account is the account of the customer or others with the owner of the business; in the Balance Sheet the account is the opposite—that is to say, the account of the owner of the business with the customer and others. Those to whom I am debtor are my creditors; in my Ledger they appear as creditors, for the Ledger shows their relation to me. In my Balance Sheet I state my relation to them, which is that of debtor, so I put them upon the left-hand, or *Dr.*, side. Therefore, when you have made out the Trial Balance from the Ledger you must, of course, transpose the sides to make the Balance Sheet." It is, of course, not impossible to prepare an account, in the form of a Ledger Account, showing the position of affairs between the sole proprietor of a business and that business; but it is an entire fallacy to suppose (as appears to have been supposed above) that the proprietor, or proprietors, of a business, and the business itself, are interchangeable terms. The accounts of a business

are the accounts of that business, and *not* the accounts of its proprietor or proprietors, and a clear appreciation of this fact will often save confusion. In the lecture already referred to Mr. COOPER went on to advise his audience never to put the words "Liabilities" and "Assets" at the head of Balance Sheets, adding that, "many years ago Sir GEORGE JESSEL severely censured this practice," and that "various items are found on both sides of Balance Sheets which are not strictly Liabilities or Assets." As no reference is given to the occasion upon which the late Sir GEORGE JESSEL "censured" this practice, comment is naturally impossible. It may be mentioned, however, that the headings deprecated by Mr. COOPER are employed in the statutory form of Balance Sheet appended to Table "A" of the Companies Act 1862. With regard to the statement that various items are found on both sides of Balance Sheets which are not strictly Liabilities and Assets, it is greatly to be feared that this is the case, but also greatly to be deplored. It is only possible to justify the inclusion of *any* item in a Balance Sheet, provided—at that time at least—it is reasonable to treat it *as* a Liability, or *as* an Asset, as the case may be. It is thought, therefore, that if these headings were in all cases attached to Balance Sheets, the incongruity of non-permissible items might be emphasised—a result which would certainly not have drawn the "censure" of the authority referred to.

CAPITAL.—Upon the liability side of a Balance Sheet the most prominent item—in the case of a limited company at least—is the shareholders' capital, which, of course, can only be increased beyond its original limit, or reduced, after due compliance with important legal technicalities. In stating the Capital Account it is desirable to show, first, the nominal capital, *i.e.*, the limit sanctioned by the memorandum of association; secondly, the number and value of each class of shares issued and the amount called up thereon, from which should be deducted the amount of calls in arrear, stating the number of shares upon which such calls are due. In France, and also in South America, it is usual to state the full amount of the capital issued as a liability, and the amount uncalled as an asset; but

this is not at all a desirable form to adopt, as it can hardly be said that uncalled capital is more than a contingent asset.

The next item to be stated is the amount paid up upon shares forfeited, when such shares have not been reissued by the company. When they are reissued this item may appropriately be absorbed in the Reserve Fund.

DEBENTURES.—Next comes the amount due upon debentures, the amount extended being the nominal amount; or, in the case of debentures issued at a discount, the amount actually received. In the latter case, however, the nominal amount should also be stated, and in both cases the rate of interest should be mentioned. Sometimes the full face value of the Debentures is shown as a liability and the amount of the Discount as an "asset"; if this plan be adopted, care must be taken to see that the latter item is properly and clearly described. The appropriate place for premiums received upon issues of either shares or debentures is in a special Reserve Fund.

MORTGAGES.—The next item upon the Balance Sheet will be the amount due upon mortgage, which, like most debentures, constitutes a preferential liability, and ordinarily speaking is practically permanent. The rate of interest should be stated here also.

OTHER LIABILITIES.—Next come the ordinary liabilities of the company, which, according to Table "A," are separated under the following sub-headings:—

- (a) Debts for which acceptances have been given.
- (b) Debts to tradesmen for supplies of stock-in-trade and other articles.
- (c) Debts for law expenses.
- (d) Debts for interest upon debentures and other loans.
- (e) Unclaimed dividends.
- (f) Debts not enumerated above.

It has become a very general practice for the item “(d) Debts for interest upon debentures and other loans” to be shown as an addition to the loans themselves. There is, of course, no possible objection to this proceeding from an accountant’s point of view ; and, indeed, this seems to be the proper place for it.

RESERVE FUNDS.—The next item upon the liability side is for “Reserve Fund, showing the amount set aside from profits to meet contingencies.” This, perhaps, is as good a definition of a Reserve Fund as has been offered, and although special Reserve Funds may be created for the purpose of providing for special contingencies, it may be taken as an axiom that no sum which is not set aside *from profits* can properly be called a Reserve Fund. Nevertheless, under the heading of “Reserve” all sorts of items are frequently included which under no possible circumstances can be considered to have been set aside out of the profits. This, perhaps, raises the somewhat large question as to what *are* actual profits, but it must at least be admitted that the term “Reserve Fund” is by no means applicable to all the following :—

(a) A sum set aside to meet Depreciation of property, and to provide for its future renewal. This is a charge against profits, rather than a sum set aside out of profits.

(b) A sum set aside for the purpose of equalising the charge against Profit and Loss for Repairs and Replacement of Machinery, &c. This, also, would appear to be a charge against profits.

(c) A Reserve to provide for loss upon Bad Debts or Depreciation of investments would likewise appear to be a charge against profits, unless, indeed, the amount so set aside was more ample than the circumstances of the case necessitated ; and in this case it would probably be a better course to charge against profits what might be considered a fair Reserve for loss, and to accumulate any further Reserve that might be thought prudent in the form of a Reserve Fund pure and simp’le.

(d) Investment Fluctuation Account. This is an item which, unless further explained, should never appear upon the face of a Balance Sheet, and that for the simple reason that its meaning is by no means clear. It may mean that investments have been re-valued at a higher figure than cost price, and the proceeds carried to this account rather than to the credit of Profit and Loss or Reserve Fund; or, on the other hand, it may mean that the investments are stated in the Balance Sheet at a higher figure than their actual value, and that the amount of the Investment Fluctuation Account is an amount set aside in anticipation of future loss. The former is a perfectly legitimate form of special Reserve Fund; the proper place for the latter (which is, in fact, merely a Depreciation Account) appears to be in reduction of the stated value of the assets.

(e) Sinking Fund, or an amount set aside (and specifically invested) for the purpose of meeting a future loss upon redemption of debentures issued at a discount, renewal of leases, &c.

(f) The so-called "Reserve Fund" of a life assurance company, which really amounts to a fund set aside out of the surplus premiums paid by the assured in the earlier years of their insurance to meet the deficiency of such premiums to cover the increased risk of later years, when the expectation of life is shorter. To a very large extent the Reserve Funds of life assurance companies are "premiums paid in advance," rather than "accumulated profits."

There can be no doubt but that it is improper to state as a Reserve Fund any sum which has not been actually set aside, out of profits, *solely* for the purpose of providing against unforeseen contingencies.

THE INVESTMENT OF RESERVE FUNDS.—So much has been written upon the "fictitious" nature of all Reserve Funds that are not actually invested in securities outside the business itself that it seems desirable, in a work of this

character, to examine the arguments that have been raised in support of this contention. So far back as 1890, Mr. T. A. WELTON, F.C.A., expressed his views upon this subject in the following terms: "The expediency, or otherwise, of making special investments of reserved profits can only be determined after a careful review of the circumstances in each particular case. I lay the more stress upon this matter because it has become the fashion in some quarters to urge that all reserves, including those of banking companies, should be specially invested, without any regard to the nature of the prospective requirements to meet which they are provided." It is believed that at that time the soundness of such views was not really seriously disputed by any very considerable section of either the Press or the public; but the numerous failures that occurred during the years 1892 and 1893 showed that the mere existence of a large Reserve Fund did not in itself suffice to ward off disaster, and hence (being in somewhat of an unreasoning mood) many unfortunate shareholders hastened into print with the view that these "paper reserves" were "fictitious." Most of the lay Press took up the cry, and their arguments—which, it must be admitted, were somewhat plausible—have now sunk so deeply into the public mind that it is not unlikely that the misconception will prove ineradicable.

At the same time it cannot be too strongly advanced that the question as to whether or not any given Reserve Fund is represented by assets consisting of marketable securities outside the business, or by less readily marketable assets employed in the business as fixed (or working) Capital, is comparatively speaking of little importance. The most casual perusal of any Balance Sheet will show at a glance, even to the least informed, by which class of assets the Reserve Fund is represented. Consequently the occasion does not arise to deal specifically with this point. What is of infinitely more importance, and what cannot be gathered even by the most expert accountant by a perusal of the published accounts, is whether the so-called Reserve Fund is (1) a *bonâ fide* accumulation of divisible net

profits set aside (or reserved) merely to provide for unforeseen contingencies, or in general terms because it is thought inexpedient to divide profits up to the hilt; (2) a Reserve set aside out of profits with a view to retaining in the possession of the company assets that may hereafter be applied to a foreseen and specific purpose—as, for example, the repayment of redeemable debentures; or (3) a provision, falsely called Reserve Fund, set aside by charging from year to year something against profits for the purpose of building up a provision to meet a known or expected deterioration of assets in the future. No mere inspection of any published accounts would enable anyone to determine to which of these three classes an item described as “Reserve Fund” belongs: hence the extreme importance, from the Auditor’s point of view, of the adoption of a correct nomenclature. The term “Reserve Fund” without qualification, ought, it is submitted, in all cases to refer solely to class (1) mentioned above. If the Reserve Fund be an accumulation of divisible profits “earmarked” in advance for a specific purpose, and therefore not properly available for any other purpose (as in the case of class (2)), the limitations of that Reserve Fund ought to be clearly stated upon the face of the Balance Sheet (*e.g.*, “Reserve Fund accumulated to provide for Redemption of debentures in 190—,” or “Reserve Fund specifically earmarked.” If a credit balance that properly comes under the definition of class (3) is called “Reserve Fund,” it is submitted that the accounts are to that extent false and misleading, and that the Auditor should require them to be amended, so that they may properly disclose the true position of affairs. If his reasonable requirement in this respect be refused, his only alternative would appear to be to place a certificate at the foot of the Balance Sheet, to the effect that his requirements, as Auditor, have not been complied with in this respect—dealing, of course, fully with the subject in his report to the shareholders.

UNDIVIDED PROFITS.—The last item upon this side of the Balance Sheet is the balance of undivided profit. It is thought preferable to show this balance without elaboration upon

the Balance Sheet and in a "Profit and Loss Apportionment Account" (or the last section of the Profit and Loss Account) to show the connection between the balance shown upon the Balance Sheet and the balance of the Profit and Loss Account for the current period. There is, however, no objection to showing the details upon the Balance Sheet, except that it does not appear to present the facts of the case so clearly.

CONTINGENT LIABILITIES.—With the question of Contingent Liabilities it is not necessary to deal at length, beyond stating that all such liabilities as are known should be noted upon the Balance Sheet, even if it is anticipated that they will not ultimately result in a claim against the company.

THE ASSETS SIDE.—Turning now to the assets, it is convenient to deal with these—as with the liabilities—under their various heads.

FIXED ASSETS.—"Table A" deals first with "Freehold Land," "Leasehold Land," and "Leasehold Buildings," which it requires to be stated separately, and apparently without deduction for depreciation. The word "apparently" is used advisedly, for depreciation is not here mentioned, although it is specifically provided for in the case of "Stock-in-trade" and "Plant." This seems to show that, even in accounts stated upon the Single Account System, the Legislature did not intend to make it compulsory for the permanent assets of a company to be re-valued periodically; and this, it will be remembered, is a question with two sides to it, viz., the possibility of a rise in value, and the possibility of a fall. Had leaseholds been excepted, it might reasonably be assumed that it was intended that companies should not allow either a rise or fall in their permanent assets to modify their trading profits; but it is impossible to suppose that the depreciation of leaseholds was intended to be ignored, and therefore the whole point remains (as it must remain until the question is definitely settled by a further enactment) extremely uncertain, so far as the legal

obligations of a company are concerned, although there need be no uncertainty as to what is the most prudent course to adopt.

FLOATING ASSETS.—Next in order “Table A” states Stock-in-trade and Plant, “the cost to be stated, with deductions for deterioration in value as charged to Reserve Fund or Profit and Loss.” It would have seemed more natural to have placed Plant before Stock-in-trade, as being obviously a “fixed asset,” and it seems strange to talk of a “deduction for deterioration in value, as charged to the Reserve Fund.” Inasmuch as the Reserve Fund has already been defined as “an amount set aside from profits to meet contingencies” the deductions that may properly be charged against Reserve Fund would appear to be limited to unforeseen deterioration, rather than for regular depreciation.

Next come “Debts owing to the company,” which for some inexplicable reason appear to be stated under separate headings, instead of being under sub-headings, as in the case of the debts owing by the company. The headings are as follow :—

Debts considered good, for which the company holds bills or other securities.

Debts considered good, for which the company holds no security.

Debts considered doubtful and bad.

It is also provided that “any debt due from a director or any other officer of the company is to be separately stated.”

It is not usually considered desirable to separately state the amount of the doubtful and bad debts, but the provision for the separate statement of any debt due from a director or other officer is one that should not be lost sight of ; doubtless, it is not intended to apply in the case of debts for small amounts in the regular course of business, but cases will readily occur to the reader in connection with some recent failures where the compliance with this provision might have materially affected the course of events.

The next item on the Balance Sheet is Investments, which should be stated in some detail, and if the investments are on account of Reserve Fund or Sinking Fund the circumstance should be clearly stated. The Life Assurance Companies Act 1870 provides the following subdivision of the item Investments upon the Balance Sheets of Life Assurance Companies, and the example is worth following under all ordinary circumstances:—

British Government Securities.

Indian and Colonial Securities.

Foreign Government Securities.

Railway and other Debentures and Debenture Stocks.

Railway Shares (Preference and Ordinary).

House Property.

Other Investments (to be specified).

It would, however, seem desirable in many cases to state the actual investments separately, for when it is remembered that such an item as "Foreign Government Securities" may include investments so various as French Rentes, Turkish Bonds, and South American Republic Bonds, it is obvious, in this case at least, the particular heading adopted is no indication whatever to the general desirability of the investment. Again, "Railway Shares" may mean anything between Great Western Stock and Grand Trunk Stock, to say nothing of Mexican and other similar railways.

Last upon the Assets' side is the item of Cash, which is best separated into—

Amount at Bankers on Deposit, including accrued interest.

Amount upon Current Account, and

Amount in hand.

GENERALLY.—It is hardly necessary to enter in detail into the forms of Balance Sheets required for different classes of undertakings; the same rules will apply in almost all cases, and although modifications of detail will appear desirable in almost

each particular case, these naturally must be considered and dealt with according to the particular circumstances that obtain, the general principle in all cases being that the accounts must be not only correct, but also so clear as to render misapprehension impossible, even among those who do not profess to be skilled accountants. In this respect it is, perhaps, well to bear in mind the particular classes of persons who are likely to be interested in the accounts. Thus, in the case of a friendly society, lucidity will be the great thing to be aimed at; while in the case of such an institution as a bank the main object of the Balance Sheet is, perhaps, less to inform shareholders as to the amount of their profits than to allow the public to form a reliable estimate upon the bank's stability. It may be added that an "account" is not primarily a collection of *figures*: it is a narration of events and facts: while a person appointed to hear and approve such narration is called an "Auditor." The importance of these points lies in the circumstance that, although accounts are now written (or printed) instead of being delivered orally, the narration (or wording) is at least as material as the figures themselves.

The following three general forms of Balance Sheets are designed for use under different circumstances:—

PRO FORMA BALANCE SHEET OF A GAS AND WATER COMPANY.
(DOUBLE ACCOUNT SYSTEM.)

Dr.

CAPITAL ACCOUNT ON 31ST DECEMBER 1906.

Cr.

Expendi- ture to 31st Dec. 1905	Expended this year	Total to 31st Dec. 1906		Certified Receipts 31st Dec. 1905	Received during year	Total Receipts to 31st Dec. 1906
£ s d	£ s d	£ s d		£ s d	£ s d	£ s d
GAS.						
To Expenditure to 31st December 1906—						
Lands acquired (including Law						
Charges)	432 0 0	25 0 0	457 0 0	40,000 0 0	..	40,000 0 0
New Buildings, Manufacturing Plant,				27,500 0 0	17,500 0 0	45,000 0 0
Machines, Storage Works, and				12,500 0 0	..	12,500 0 0
other Structures connected with						
manufacture	26,807 0 0	4,395 0 0	31,202 0 0			
New Mains and Pipes, including						
laying of same, paving, and other	14,161 0 0	859 0 0	15,020 0 0			
works connected with distribution	600 0 0	130 0 0	730 0 0			
New Meters, including fixing ..	2,000 0 0	591 0 0	2,591 0 0			
Cost of promoting special Act ..						
Total Gas	£44,000 0 0	£6,000 0 0	£50,000 0 0			
WATER.						
To Expenditure to 31st December 1906—						
Lands acquired (including Law						
Charges)	216 0 0	..	216 0 0			
New Buildings, Storage, and Filtra-						
tion Works, and other Works con-	12,886 0 0	4,637 0 0	17,523 0 0			
nected with collection of water ..						
New Mains, including laying of						
same, paving, and other works	19,706 0 0	1,939 0 0	21,645 0 0			
connected with distribution ..	2,067 0 0	1,739 0 0	3,806 0 0			
Cost of promoting special Act ..						
Total Water	£34,875 0 0	£8,315 0 0	£43,190 0 0			
Balance of Capital Account ..	1,125 0 0	3,185 0 0	4,310 0 0			
	£80,000 0 0	£17,500 0 0	£97,500 0 0	£80,000 0 0	£17,500 0 0	£97,500 0 0

GENERAL BALANCE SHEET ON 31ST DECEMBER 1906.

				£ s d							£ s d							
CAPITAL ACCOUNT—																		
Balance to credit thereof (Account C)				4,310	0	0	CASH AT BANKERS..				3,239	0	0
PROFIT AND LOSS ACCOUNT—																		
Balance to credit thereof (Account E)				4,179	0	0	COALS, for stock on hand 31st December 1906				..	365	0	0	
RESERVED FUND—																		
Balance to credit thereof (Account F)				2,225	0	0	COKE, TAR, &c. ..				..	118	0	0	
DEPRECIATION FUND (for works on Leasehold Lands)—																		
Balance to credit thereof (Account F*)				775	0	0	GENERAL STORES ..				..	1,445	0	0	
INTEREST ACCRUED AND UNPAID ON DEBENTURE STOCK TO 31st December 1906							GAS AND METER RENTAL, Balance of this Account due to the Company on 31st December 1906				..	428	0	0	
SUNDRY TRADESMEN AND OTHERS—																		
For amount due for Coals, Stores, &c., to 31st December 1906				312	10	0	GAS FITTINGS, do.				..	444	0	0	
WAGES AND SUNDRIES				COKE AND OTHER RESIDUALS				..	436	0	0	
										WATER RENTAL, do.				..	700	0	0	
										WATER FITTINGS, do.				..	825	0	0	
										RATES AND TAXES, paid in advance				1,525	0	0
										INVESTMENTS (specified)				147	0	0
																3,600	0	0
																£15,000	0	0

PRO FORMA BALANCE SHEET OF A MANUFACTURING COMPANY.

(SINGLE ACCOUNT SYSTEM.)

BALANCE SHEET, 31st DECEMBER 1906.

<i>Liabilities</i>		£	s	d	<i>Assets</i>		£	s	d	£	s	d
Nominal Capital (10,000 Shares of £10 each)	..	100,000	0	0	Leasehold Buildings at—(at cost)	..	..	..	..	10,000	0	0
Capital Subscribed (5,000 Shares of £10 each, £8 per Share called up)	..	..	..	..	Less Depreciation	..	..	..	..	1,218	0	0
Less Calls in arrear	..	40,000	0	0	Plant and Machinery—	..	..	..	..	20,000	0	0
Debenture Stock (at 4½ per cent.)	..	250	0	0	Value, 1st January 1906	..	..	..	..	1,800	0	0
Bills Payable	..	..	..	..	Additions during the Year	..	..	..	..	21,800	0	0
Sundry Creditors	..	..	..	..	Less Depreciation	..	..	..	..	2,000	0	0
Interest on Debentures	..	..	..	..	Warehouse and Office Fittings—	..	..	..	..	250	0	0
Unpaid Dividends	..	..	..	..	Value, 1st January 1906	..	..	..	..	31	5	0
Reserve Fund	..	..	..	..	Less Depreciation	..	..	..	..	..	..	..
Profit and Loss Account (Balance available for Dividends, &c.)	..	..	..	..	Stock-in-Trade (at cost), viz.—	..	..	..	..	6,000	0	0
					Materials	..	..	..	..	9,000	0	0
					Goods Unfinished..	..	..	..	..	15,000	0	0
					Manufactured Goods	..	..	..	..	..	..	..
					Bills Receivable..	..	..	..	..	..	..	..
					Sundry Debtors..	..	..	..	..	..	..	..
					Investment of Reserve Fund—	..	..	..	..	..	..	..
					£4,000 Great Northern Railway 3 per cent.	..	..	..	..	..	..	..
					Debenture Stock, at par.	..	..	..	..	..	..	..
					Cash—	..	..	..	..	..	..	..
					At Bank	..	..	..	..	1,281	3	9
					In hand	..	..	..	..	200	0	0
										1,481	3	9
										£91,751	18	9

CONCLUSION.—In considering these matters, however, it must be borne in mind that it is very exceptional for the form in which accounts are stated to be actually under the control of the Auditor. As a rule, articles of association provide that the accounts shall be rendered in such form as the directors shall think fit, and in such cases it is, of course, impossible for the Auditor to dictate as to the precise form to be adopted. This, however, does not release him from the responsibility of judging as to the fitness of the form in which the accounts are rendered by the directors. In this respect he is placed in a position and furnished with information which is withheld from the general body of the shareholders, for the express purpose of satisfying himself that the accounts submitted by the directors to the shareholders are such as will reasonably disclose the position of the company. Considerations with regard to the form which the accounts should take are frequently of a nature which the Auditor must of necessity weigh for himself; for, inasmuch as the shareholders have no knowledge of the transactions or position of the company other than that which they gain from a perusal of the directors' accounts and the Auditor's report, it stands to reason that if the accounts do not sufficiently disclose these things it may frequently happen that the shareholders themselves would have no reason to suspect that the accounts were not all that they should be. It therefore follows that, although the Auditor does not have the drafting of a company's accounts, it is necessary for him in all cases to consider the form in which they are submitted for his approval, and not merely to content himself with an examination of their technical correctness. It has been stated by some that, the accounts submitted to the shareholders being the accounts of the directors, they, and they only, are responsible to the shareholders for the form. This is true to the extent that the Auditor has no power to compel the directors to modify the form of their accounts; but it is not true in the sense that if the accounts submitted are, so far as they go, correct, the Auditor is under no responsibility to specially report in such cases as they are insufficient to enable anyone examining them to obtain a correct idea of the

company's position. Were this the case it would indeed be difficult to see in what respect the shareholders gained by an audit of their accounts, for it is obvious that it would be possible to conceal almost anything in the shape of fraud or unjustifiable extravagance. The shareholders have, however, a clear right to such accounts as will enable them from time to time to judge of the value of their investment ; and it is for the purpose of making the accounts reliable for this purpose that an Auditor is appointed. And while there rests with him the serious responsibility of concealing such matters of internal detail as would, if divulged, tend to damage the position of the business, yet, on the other hand, he must not fail to remember that it is the shareholders, and not the directors, who are the masters of the fortune of the company, and that (except in matters of internal detail) they have an indisputable right to the fullest and clearest information.

CHAPTER VIII.

WHAT ARE PROFITS ?

IN the preceding chapters most of the points arising in the course of an audit, with a view to ascertaining that all due precautions have been taken to test the accuracy of accounts before certifying them, have been considered in some detail; but it is advisable to review some of these various questions from the point of view of considering whether or not the amount of profit stated upon the face of the accounts is actually available for dividend. It is most important to remember in this connection, however, that until an undertaking has been actually wound up, any statement as to the profits earned is merely an estimate, or a statement of opinion, and not a question of fact.

ADVANTAGES OF DOUBLE ENTRY.—The reader will hardly require to be reminded that, in the case of an ordinary undertaking, the amount of profit available for distribution will be represented on the Balance Sheet by the excess of the assets there disclosed over the liabilities and paid-up capital of the undertaking. But it is desirable for the Auditor, in order to make sure of his position, to look at the matter not merely from a Balance Sheet point of view, but, in the first place, to carefully scrutinise the Revenue Account in order to see that no sources of income have been taken credit for unduly, and that all reasonable expenses have been properly debited, and then to compare the profit shown by such Revenue Account with the surplus before mentioned, stated to be available on the face of the Balance Sheet, after scrutinising all the assets and liabilities

there disclosed. By this means he will have the advantage of looking at the matter from two points of view, which, in so difficult a question as the assessment of actual profits, is of the utmost value.

CAPITAL v. REVENUE.—It will be seen from what has been said above that, at all events economically speaking, no profits are available for distribution until provision has been made for keeping the whole of the paid-up capital of the undertaking intact. The absolute necessity for this provision has, however, been rendered somewhat doubtful by many decisions which have been given in the Courts from time to time. Foremost among these may be named the following:—*Lee v. The Neuchâtel Asphalte Company, Lim.*, *Verner v. Commercial and General Trust, Lim.*, *Wilmer v. McNamara & Co., Lim.*, and *Dovey v. Cory (In re The National Bank of Wales, Lim.)*; all of which will be found reported in full in Appendix "B" to the present work. It may be stated in this connection, however (although necessarily shortly and incompletely), that the effect of all these decisions was that *under certain circumstances it might not be necessary* for a company, before declaring a dividend out of profits alleged to have been earned, to provide in that year's accounts for the whole of the loss caused by the shrinkage in intrinsic value of the whole or a portion of its assets. In the case of *Lee v. The Neuchâtel Asphalte Company, Lim.*, it is true that the actual facts disclosed did not place it beyond doubt that the fixed assets of the company were in fact less valuable than when they were taken over in the first instance; but in the three later cases the fact that some depreciation had occurred was undisputed, and although some provision had been made for this depreciation in the two last-named cases, it was not seriously contended that a sufficient sum had been written off to cover the whole of the loss.

On the other hand, it is very desirable that no undue importance should be attached to these decisions, for it must be remembered that the first three arose out of a motion upon the part of one or more shareholders to obtain an injunction against

the directors of a company, restraining them from declaring a dividend ; and that, in the absence of any evidence that creditors would be defrauded, or the rights of one or more classes of shareholders seriously prejudiced, the Courts would naturally not lightly interfere with the deliberate action of the directors, endorsed by a resolution of the company passed in general meeting, in regard to a matter which would certainly appear to be essentially one of internal administration. The last decision (*In re The National Bank of Wales, Lim.*) arose out of a misfeasance summons, and the main question was thus as to whether the respondent was responsible for the position of affairs disclosed.

The most difficult questions that arise under this heading proper occur in the case of a company which has sold a part of its undertaking, but the general principles to be applied in such cases have been fairly well defined by the Courts. In the case of *Lubbock v. British Bank of South Africa, Lim.*, it was decided by CHITTY, J., in 1892, that so long as it was not *ultrâ vires* the company, a profit made on the sale of part of the undertaking was available for dividend—upon the principle, apparently, that there was nothing in the Companies Acts themselves to prevent a company declaring that one of the “objects” for which it was incorporated was to from time to time, as opportunity offered, sell at a profit undertakings which had in the first instance been acquired not for the purpose of re-sale, but with the idea of working them for revenue purposes. That is to say, there is no statutory provision to prevent a company from changing its mind, and deliberately converting fixed assets into floating assets. To some extent, however—although to no unreasonable extent—this somewhat general decision was limited by the late Mr. Justice BYRNE in the case of *Foster v. The New Trinidad Lake Asphalt Company, Lim.*, decided in 1900. Shortly stated, the position here was that the company had in the first instance acquired a number of miscellaneous assets for a lump sum, and had—doubtless in the exercise of a *bonâ fide* discretion vested in the directors—apportioned the purchase-price over the various assets so acquired. One of these assets seems to have been a

book debt of an extremely doubtful nature, which was valued at *nil*, but which eventually produced to the company the sum of £26,258 16s. The directors sought to regard the *whole* of this sum as profit, doubtless on the footing that the asset in question had cost the company nothing and that therefore whatever it actually realised was clear profit. On a motion on behalf of debenture-holders and a shareholder to restrain the application of these moneys to the payment of a dividend, his Lordship made an order in the terms applied for. In doing so, however, he said "It is clear, I think, that an appreciation in the total value of capital assets, if duly realised by sale or getting in of some portion of such assets, may be a proper case to be treated as available for purposes of dividend"; but he held—and accountants will doubtless agree with his holding—that so material a disproportion between the directors' original apportionment of the purchase-price among the assets acquired and the realisable value of one of those assets clearly suggested that, before any such alleged profit as that referred to can be safely treated as true profit, the whole business of the apportionment of the purchase-price ought to be gone over afresh. Had the directors been prepared to re-value all their fixed assets, and after such re-valuation to only treat as profit the excess of the *bonâ fide* value of the fixed assets retained, *plus* the proceeds of assets realised, over the original costs of all assets as profit, there can, it is thought, be but little doubt that his Lordship would have sanctioned a dividend paid out of profits so computed.

Another decision that ought not to be overlooked in this connection is that of Lord (then Mr.) Justice FARWELL in the case of *Bond v. Barrow Hamatite Steel Co., Lim.*, decided in 1902. It is thought that most accountants will find the greatest difficulty in accepting the principle apparently enunciated by his Lordship, that "fixed" and "floating" assets are interchangeable terms. Getting down to first principles, it is clear that any company might always carry on its business without any fixed assets at all, by the simple expedient of hiring those assets for a periodical consideration, or rent; and that therefore whenever,

instead of hiring, a company decides to buy, it *pro tanto* embarks upon an additional business, or department of its business. But the mere fact that an undertaking decides to acquire fixed assets, and thus make itself independent of other undertakings, does not *ipso facto* convert the assets so acquired into floating assets, merely because, had they remained in the ownership of other undertakings which had hired them to this undertaking, they might possibly have been regarded by them as floating assets. The proper distinction between fixed and floating assets must, it is thought, always rest with the *intention* of the parties owning such assets, and the manner in which they propose to utilise them; and although it may be permissible for an undertaking to change its views with regard to particular assets from time to time, provided such change of views be made *bonâ fide*, the suggestion that no real distinction between the two classes of assets exists is one that can produce nothing but confusion. However, in spite of the utter fallacy of his Lordship's argument, it is thought that no fault can be found with the general conclusions arrived at. The *crux* of the case that Mr. Justice FARWELL had to decide was as to whether the shareholders of a company, or any class of shareholders, had an absolute inalienable right to dividends out of profits which had clearly been earned; or whether the position was not that it was for the company in general meeting (subject to such limitations as might have been imposed by its articles) to decide what dividends were to be paid, leaving to individual shareholders merely such rights of preference *inter se* as the articles might have provided. This latter, no doubt, is a correct interpretation of the position. Preference shareholders have a right to their prescribed preference dividend before more deferred shareholders receive anything whatever; but they have themselves no right to receive anything by way of dividend until it is duly voted to them. In an extreme case, if it could be shown that a majority of ordinary shareholders were corruptly taking advantage of their statutory rights to defraud a minority of preference shareholders, a Court of Equity might no doubt intervene; but it would require a very strong case before the Courts would interfere between two classes

of shareholders in so purely a domestic matter as the treatment of available profits.

DEFINITION OF "PROFITS."—In connection with the question as to what are profits available for distribution, it is of interest to note the definition given in *Buckley*, which is as follows:—"The profits of an undertaking are the excess of revenue receipts over expenses properly chargeable to Revenue Account. It is impossible to lay down any general rule as to what expenses are chargeable to revenue and what to capital."

It will probably be admitted that this is one of the most diplomatic definitions that has ever been given upon a subject of such vast importance; inasmuch as it leaves the inquirer exactly where he started, for it still remains for him to define what receipts are attributable to capital and what to revenue, and what expenses are attributable to capital and what to revenue. Could these questions be definitely answered in each case, it is obvious that the question of what the actual profits have been would be one capable of the most ready solution.

Another dictum—namely, that of Lord Justice LINDLEY in the *Neuchâtel* case—is of considerable importance, not because it tends to clear up the difficulties which have been mentioned above, but because it unquestionably adds to them. Lord Justice LINDLEY stated that "It is said that such a course involves payment of dividends out of capital—the answer is that the Acts nowhere prohibit such a payment as is here supposed. The proposition that it is *ultrâ vires* to pay dividends out of capital is very apt to mislead, and must not be understood in such a way as to prohibit honest tradings. It is not true as an abstract proposition that no dividends can be properly declared out of moneys arising from the sale of property bought by capital. But it is true that, if the working expenses exceed the current gains, profits cannot be divided, and that if in such a case capital is divided and paid away as dividend the capital is misapplied, and the directors implicated in a misapplication may be compelled to make good the amount misapplied." Were

the above to be regarded as a final statement of the law upon the subject, it would appear to follow that there is nothing whatever to prevent a company selling a portion of its undertaking and distributing the purchase-money by way of dividend among its shareholders. This, however, would appear to be, at all events, one of those particular conditions which the Companies Act 1877 was expressly formed to meet, when it provided that, under such circumstances as this, a company might return to its shareholders a portion of their paid-up capital, and reduce its capital accordingly. If such return can be made to shareholders without any reduction of capital, it would seem that the time of the Legislature was wasted; and although it is true that for all practical purposes this Act has proved to be almost a dead letter, yet it is difficult to accept the suggestion that it has added *no* powers which did not previously exist in connection with company finance.

Until quite recently it was very generally thought that no scheme for the reduction of a company's capital could be carried until it had been shown that a Balance Sheet, prepared upon reasonably proper lines, showed a corresponding deficiency of assets: that is to say, the view ordinarily held was the one already mentioned in these pages that losses on Revenue Account were chargeable first against current gains, secondly, against prior accumulations of profits (including Reserve Fund), and finally against capital, in which last case only, and to which extent only, could a scheme for the reduction of a company's capital be carried through. If the capital of a company consisted only of one class of shares there can be but little doubt that these principles would still be maintained; but in *In re Hoare & Co., Lim.*, which came before the Court of Appeal in 1904, a different, and somewhat unusual, position of affairs transpired. In this case the Reserve Fund represented chiefly the accumulation of premiums received on the issue of preference shares; the directors held all the more deferred classes of shares, and under the circumstances which obtained they recognised that the whole of the loss which had in point of fact taken place ought equitably

to fall upon them. They accordingly propounded a scheme for the reduction of capital which conformed to this entirely reasonable—if magnanimous—point of view; and their scheme was rejected by Lord (then Mr.) Justice BUCKLEY, solely because he considered that he had no jurisdiction to approve a scheme for the reduction of capital which did not involve the whole of the accumulated Reserve Fund being previously written off. The Court of Appeal, however, took a somewhat wider view of the jurisdiction of the Court in the approval of such schemes, and sanctioned the one before them on its merits. It is thought, however, that their decision (while beyond criticism from a business point of view) ought not to be regarded as in any way affecting the general statement of principle that Reserve Funds represent accumulations of divisible profits, which are accordingly at all times available for dividend, subject to the prior liability of making good any losses on account of Revenue that may occur while they remain undistributed.

Another point that should be borne in mind in this connection is that under all normal circumstances *bonâ fide* profits on Revenue Account may be reasonably expected to recur from year to year, and that, therefore, dividends paid out of revenue ought to be capable of being easily maintained out of revenue, provided the management continues to be equally successful and no untoward circumstances obtain. Profits on account of capital, however—whether they come strictly under that definition and are, therefore, not legally available for dividend, or whether they come upon the border-line and are legally (although not prudentially) so available—are, in the nature of things, not likely to regularly recur from year to year. Hence, even if it be legal to distribute such profits by way of dividend, it is clear that in the future such dividends cannot be reasonably expected to be maintained. This is, perhaps, one of the most powerful practical reasons that can be put forward in favour of such profits not being paid away as dividends. If the moneys that they represent cannot be usefully employed in the business, and are not required for Sinking Fund purposes, it may be that there is practically

no alternative but to divide them ; but in such cases it is thought that the division should be by way of Bonus, and not by way of Dividend, with a view to emphasising the facts (*a*) that the distribution in question is not on account of current profits, (*b*) that it cannot be expected to regularly recur. These, however, are, of course, questions for the management and not for the Auditor, who is in no way concerned with the management of the undertaking. At the same time it is usually practicable for the Auditor, by the use of his influence, to discourage extremes of imprudence, and thus prevent the disappointment which must inevitably follow the imprudent methods already referred to.

REVENUE RECEIPTS.—These somewhat exceptional points being thus disposed of, the right conception of the effect of more ordinary transactions may now be considered. For this purpose it will be convenient to classify the various items appearing upon both sides of a Revenue Account, which in the aggregate show the profit alleged to be available for dividend. Upon the credit side these items may be conveniently classified under the following headings:—

- (*a*) Profit on transactions completed but not yet received in cash.
- (*b*) Profit on transactions not completed, whether received in cash or not.
- (*c*) Profit on transactions completed and received in cash.
- (*d*) Profit arising from an estimated rise in the value of fixed or floating assets.
- (*e*) Profit not properly incidental to the nature of the business carried on.

With regard to (*a*) it is hardly necessary to add to what has been already said in the preceding chapters, but the principles there enunciated may be summarised as follows:—It is necessary to consider

- (1) Whether it may be fairly and reasonably anticipated that the debt will be discharged in due course.
- (2) Whether any allowance or discount is likely to be claimed when the debt is discharged ; and
- (3) Whether it is necessary to allow for the loss of interest incidental to the deferred payment of such debt.

The points which arise on (*b*) have already been very fully considered under the headings of "Work in Progress," and "Goods sold for future delivery." It is therefore unnecessary to go further into detail in the present chapter. It may be added, however, that, in the case of financial companies underwriting issues of shares or debentures, it would appear to be clearly improper to take credit as a profit for any commission upon such underwriting in respect of that portion of the issue which had been allotted to—and still remained in the hands of—the company by reason of the subscriptions from the general public being insufficient. The nature of an underwriting agreement is that, in consideration of a certain commission, the underwriter agrees to take up a certain portion of the issue if the public do not subscribe enough among them to take up the whole amount among themselves. In the event of the public subscriptions being insufficient, therefore, the contract has the effect of the underwriter acquiring a certain portion of the issue at a discount ; and that is the view which, it is submitted, the Auditor should take of the transaction. If this view be adopted, it necessarily follows that until such shares or debentures are disposed of they should appear as an asset in the accounts of the underwriter, not at their face-value, but at cost price ; that is to say, the underwriting commission should be dealt with, not as a profit, but as a reduction from the actual cost of the shares or debentures, as the case may be. *A fortiori* if assets are sold for payment in "paper," no profit should be taken credit for until that paper is actually realised in cash.

(*d*) Although the effect of Mr. Justice ROMER's decision in the case of *Bolton v. The Natal Land and Colonisation Com-*

pany, Lim., would appear to be that a company may take credit for an assumed rise in the value of its floating assets, should it think it expedient so to do, it is thought that accountants, as a body, will be more inclined to take the view that any profit arising in respect of dealing in such assets should only be taken credit for in the period during which such dealing actually occurs. That is to say, that assuming such floating assets have risen in value, the proper time to take credit for the profit is not when the rise may in point of fact have occurred, but at the time when such assets are sold. Taking credit for profit arising from an assumed appreciation in the value of fixed assets is expressly forbidden by the decision just referred to, a full consideration of this point would, however, appear to be more conveniently dealt with under the following heading.

(e) Article 73 of Table "A" of the Companies Act 1862 provides that "no dividends shall be payable, except out of the profits arising out of the business of the company"—that is to say, arising out of some transactions which come within the "objects" for which the company was formed, as set out in its memorandum of association. Inasmuch, however, as Table "A" is not compulsory, and is in the majority of cases superseded by special articles of association, it will be seen that this clause has no bearing, except upon those companies which are either registered without special articles or include in their articles a clause similar to article 73 of Table "A." Leaving upon one side the most usual source of profit of this description—viz., the sale of a portion of the company's undertaking—which has already been dealt with, the most ordinary classes of profits to come under this heading would be premiums received upon shares or debentures, and cash which has been paid up upon shares forfeited. The usual custom with both these sources of profits is to credit the amount to Reserve Fund, and it would be difficult to improve upon this. But, at the same time, it has been already pointed out that—in the absence of special articles, and in the absence of an article specially so providing—there is nothing to prevent a company transferring the whole, or a

portion, of its Reserve Fund to Profit and Loss Account, and declaring a dividend out of the increased balance so available. In this connection it is important to consider the true effect of the decisions in *Lubbock v. British Bank of South Africa, Lim.*, *Foster v. New Trinidad Lake Asphalte Company, Lim.*, *Bond v. Barrow Hæmatite Steel Company, Lim.*, and *In re Hoare & Co., Lim.*, which are fully reported in Appendix "B," and have already been discussed in the course of the present Chapter.

REVENUE EXPENSES.—Turning now to the expenses recorded upon the debit side of the Revenue Account, these may be conveniently classified under the following headings:—

- (a) Expenses that are properly chargeable to the period under review.
- (b) Expenses which may properly be spread over a term of years.
- (c) Undisclosed and contingent liabilities.
- (d) Depreciation.
- (e) Losses arising by fluctuation of floating assets.
- (f) Losses arising by fluctuation of fixed assets.
- (g) Reserves for losses.
- (h) Preliminary expenses.

With regard to (a), it is obvious that these amounts should all be charged up against the current year's revenue, and the steps which have been indicated in the preceding chapters should be taken to see that everything coming under this heading has been so charged.

(b) It should be remembered that the onus rests upon the directors and Auditor to justify this class of expenditure *not* being included as a charge against the current profits, and that the Auditor must therefore, before passing the accounts, satisfy

himself as to the sufficiency of the reasons advanced for its exclusion. Examples of items which may be properly held in suspense are dead rents paid in excess of royalties by collieries and similar undertakings, where there is a reasonable ground for supposing that they can be redeemed out of future earnings; and also special expenditure in the way of advertising some new venture or undertaking, which expenditure, it is estimated, need not be maintained after the venture has been once established. With regard to the latter, however, especial care is necessary, with a view to seeing that a sufficient sum is written off annually, as it not infrequently happens that the expectations of the managers are not realised, and that the permanent cost of advertising is far more than had been anticipated.

It is unnecessary to add anything upon either (c) or (d) to what has already been said in the preceding chapters, where both matters have already been very fully dealt with.

Passing on to (e), it may be pointed out that, inasmuch as the definition of "floating assets" is that class of assets which it is the object of the undertaking to convert with all convenient speed into cash, it is obvious that, so far as possible, nothing in excess of the actual current market value should be attached thereto upon the face of any Balance Sheet. Special circumstances may occasionally modify this, where at the moment of balancing there has been a wholly unexpected and *temporary* fall in value which has been recovered before the certifying of the accounts. It is probable, however, that it is only in connection with the treatment of foreign exchanges that this principle can generally be safely applied.

(f) Concerning this item, it is thought that, so long as the permanent earning capacity of the fixed asset has not diminished, it is quite unnecessary for any provision to be set aside, with a view to making good a loss which may have occurred by reason of the fluctuation of the value of such assets. Certainly the legal decisions which have been given under similar circumstances would appear to support this view. It is

important to remember, however, that, if the views already expressed with regard to fluctuations *upwards* in fixed assets have been disregarded, and credit has been taken for such fluctuations as a profit, then *à fortiori* is it necessary that fluctuations downwards should be given effect to.

(g) With regard to reserves for losses, as has already been pointed out, it is very important that ample reserves should be made to meet all reasonable contingencies before allocating profit for purposes of payment of dividend. The only thing that appears to call for attention here is that in some cases—although, of course, quite improperly—what is really a reserve against loss is described upon the face of a Balance Sheet as a “Reserve Fund”; under no circumstances, however, must such so-called Reserve Fund be encroached upon for the purpose of equalising dividends, unless the Auditor is satisfied that a sufficient balance remains to meet any reasonable expectation of loss that may occur.

(h) Under almost all circumstances it will be found usual to write off a portion of the amount incurred by a company in preliminary expenses, say, one-third or one-fifth, in each year's accounts until the amount is wholly extinguished. There is no compulsion, however, that this course should be adopted, although it is certainly one to be recommended; and it may be added that, should the first year's accounts show a loss, it is distinctly preferable not to obscure the actual facts of the case by increasing such loss by writing off any portion of the preliminary expenses. It is, of course, impossible to write them off except out of profits, and the attempt should, therefore, not be made upon paper. *Per contra*, where there is a Reserve Fund and the accounts for the current period show a loss, a transfer of such loss should be made to the debit of Reserve Fund, so far as the latter is sufficient for the purpose, it being a contradiction in terms to state a loss upon one side of the Balance Sheet, and a Reserve Fund (*i.e.*, an accumulation of undivided profits) upon the other side.

PROFITS PRIOR TO INCORPORATION.—In practice the contract of sale of a going business to a new company often transfers the undertaking to the latter as from a date anterior to the date when the company is entitled to carry on business: any profits earned during the intervening period must be treated as a reduction of the price paid for Goodwill; and, *per contra*, any loss sustained must be regarded as an addition to the cost of Goodwill. The necessary apportionment of profits, or losses, is not necessarily to be made *per diem*: it must be made by the directors, having regard to *all* the material facts and circumstances.

IN CONCLUSION, it may be pointed out that although the "cash" basis, as applied to commercial accounts, is in the nature of things most fallible, it has a very substantial utility, as applied to the revision of the results arrived at by means of the ordinary Revenue Account. The primary object of every Revenue Account is, of course, to arrive at the true net profit earned during the period under review; but, in the case of the vast majority of undertakings, by no means the least important use to which the Revenue Account will be put is to determine the amount of such profits *available to be drawn out of the business* and distributed among the proprietors in the case of a company or a partnership, or spent by the sole proprietor in the case of a business owned by an individual. The terms "net profit" and "profit safely divisible" are by no means interchangeable; for unless the working capital be abundant, profits cannot be prudently drawn out of the business until they have been actually realised in cash. It therefore follows that, in the great majority of cases, a safeguard—and at the same time an easily applied rough check upon the accuracy of the Revenue Account—is afforded by looking at the Balance Sheet, and seeing whether it would be practicable to draw out of the business the whole of the profits alleged to have been made, and whether there would then still remain a sufficient balance of "liquid" assets available to meet the ordinary requirements of the business. Unless such a sufficiency would remain after

dividing profits up to the hilt, it is clear that such profits have not been realised, or else that they have been diverted from their proper course and applied as working capital, in either of which events it would be impossible to distribute them without causing financial embarrassment. In this connection it is of interest to note that in the case of *Badham v. Williams* (*vide* Appendix "B") Mr. Justice KEKEWICH decided that the profits of a firm of solicitors ought to be computed on the "cash" basis.

CHAPTER IX.

THE ATTITUDE OF THE AUDITOR.

IN the foregoing chapters the object, extent, and manner of conducting an audit have been dealt with, and also—so far as the space at disposal permitted, and the general scope of this work appeared to justify—such modifications of, and departures from, the normal plan as are necessary to adapt it to the peculiar requirements of any individual audit with which the reader is likely to be concerned. The position of the Auditor himself will now be more particularly considered.

WHO MAY BE AN AUDITOR.—Auditors may, for general purposes, be divided into three classes:—

- (a) Amateur Auditors.
- (b) Professional Auditors.
- (c) Official Auditors.

It may be well to say a few words about each class before proceeding further.

AMATEUR AUDITORS are a class to whom the author has no great desire to express either affection or respect. He has seen too much of their shortcomings, and of the inexpressible misery and distress that have been caused by their scandalous incompetency, to feel any desire to deal gently with their failings. Auditing is much too serious a matter to be trifled with; the evil that can be wrought by an incompetent Auditor is hardly less vital—and is infinitely more extensive—than that which may be exercised by an unqualified medical

practitioner. The latter, if he be the possessor of an extensive practice, might possibly poison a hundred or so patients in the course of a long career; but the former can, while merely confining his attentions to the affairs of one undertaking, readily accomplish the ruin of tens of thousands and the starvation or suicide of scores in a much shorter period.

Some may think that is over-stating the case, and will say that there are many amateur Auditors who are both capable and conscientious. It is not attempted to dispute the fact that the number of amateur Auditors who are known to have failed to justify the confidence reposed in them is altogether insignificant as compared with the number who are still discharging their functions to the satisfaction of all concerned. It may, however, be remarked that "the satisfaction of all concerned" does not go for much: the Auditors of the Portsea Island Building Society, the Cardiff Savings Bank, the Rock Investment Trust, and a host of other disastrous undertakings, exercised their functions, presumably, "to the satisfaction of all concerned" (especially of the criminals) until the moment when the crash occurred: and it is worthy of note that the crash never does occur until the defalcator has taxed his milch-cow beyond its strength, and that, when it does occur, it is not the amateur Auditor who has brought it about. In fact, until the defalcator is fool enough to kill his golden goose, the amateur Auditor always does "continue to discharge his functions to the satisfaction of all concerned"; but does that prove the said Auditor to be discharging his functions either capably or conscientiously? Assuredly not.

Again, is it not a fact that, as a class, amateur Auditors have been shown (by indisputable statistics) to be more often concerned in cases of disaster than professional Auditors? Is it not almost invariably the case that, where professional Auditors are concerned, they have themselves detected the frauds, while with amateur Auditors the crash almost invariably comes from without?

As, however, this work is primarily intended for the use of professional Auditors—to whom, alone, the perusal of any book upon auditing would be likely to confer any practical advantage—the subject need hardly be pursued further. The following quotation from a lecture by the late Mr. JOSEPH SLOCOMBE, F.C.A., will, however, not be without interest in this connection. Speaking of amateur Auditors, Mr. SLOCOMBE said, some years ago: “Their number is thinning down year by year, and some of you may probably live to see the day when the amateur Auditor will be almost as extinct as the dodo. The non-professional Auditor is generally a man of business—frequently retired—whose friends think he has an aptitude for figures and investigation. Sometimes—indeed often—the friends are right, and it has been my lot to meet with non-professional gentlemen in the capacity of Auditors whose painstaking sagacity and skill would be creditable to any trained accountant: but I could tell humorous stories of another section of this class—gentlemen whose capacity for auditing the condition of the sherry (which in their case generally accompanied the audit) was doubtless excellent, but whose ability to audit any set of accounts did not exist outside the imagination of the friends who had been instrumental in their appointment. *The experience of later years has shown that unprofessional audits are generally incomplete and frequently worthless.* Worthless in cases such as I have just referred to, and incomplete—except in small matters—because the gentlemen appointed have not either the time, the inclination, or, so to speak, the machinery for that thorough examination which we know to be essential if an audit is to be effectual and reliable.”

All professional auditors would like to share Mr. SLOCOMBE'S pious hope for the ultimate extinction of the amateur Auditor; but some will doubt whether that consummation is very appreciably nearer than it was when the words quoted were spoken—more than twenty years ago. A step has, however, been made in that direction by the Building

Societies Act 1894, which requires that at least one of the Auditors of every society shall publicly carry on business as an accountant, and if accountants could only agree among themselves a further development in the right direction might reasonably be expected in the immediate future. In practice this provision is readily evaded, but it is something to note the obvious good intentions of the Legislature.

Another of the few official recognitions of the benefits of a professional audit was provided in 1898, when the Education Department issued an order requiring that the accounts of the receipts and expenditure of every School receiving a grant in aid from the Government, should be annually audited by a Chartered Accountant, an Incorporated Accountant, or in special cases (*i.e.*, presumably in rural districts where no professional accountant was available) by some other person—not being a manager or treasurer of the school—whose competency was proved to the satisfaction of the Department. The Education Acts of 1902 and 1903 have, however, placed all such schools under the control of local authorities, have abolished the professional audit, and—even in the case of those local authorities which come under the Municipal Corporations Act 1882 (and therefore are not required to submit their accounts to a Government audit)—has required that the accounts of the Education Authority are to be audited by District Auditors attached to the Local Government Board. In this respect, therefore, there has been a clear retrogression from professional to official audits.

On the subject of official audits themselves, the Report of the Joint Parliamentary Committee on Municipal Trading (reproduced on page 154) is sufficiently explicit. It has already been mentioned, however, that this Report has not been acted upon in any way. It is understood that the Local Government Board does not propose to follow the Committee's suggestion, that it should commit departmental suicide, but rather intends in the near future to seek

parliamentary sanction to an extension of its existing powers. In this connection it is significant that the question of audit was not referred to the Committee appointed in December 1905 to consider the form of Local Authorities' Accounts.

PROFESSIONAL AUDITORS are a class with whom the reader may fairly be considered to be well acquainted. Both on account of their special training, and on account of the fact that their energies are not distracted by other, and dissimilar, occupations, they are *par excellence* the ideal Auditors. Moreover, the peculiar facilities they possess, in the shape of a large staff of specially trained assistants, place them in the position to thoroughly perform audits of a magnitude that could not conscientiously be undertaken by any one man, no matter how skilled.

On the other hand, it is only fair to state that while an audit conducted by competent and responsible professional accountants is the only form of audit that can reasonably be expected to provide those safeguards which every audit ought to secure, there are some, even among the ranks of professional accountants, whose chief anxiety appears to be to disclaim any such measure of responsibility for their work. Thus it has been asserted in one quarter that "he is the worst friend of the (accountancy) profession who seeks to enlarge the responsibilities of auditors"; while the index of the 8th edition of "Auditors, their Duties and Responsibilities," by Mr. F. W. PIXLEY, F.C.A., does not comprise any such words as "Defalcations," "Fraud," or "Liabilities of Auditors"—thus clearly showing that although these matters may be dealt with incidentally in the body of the work, they were regarded as of quite second-rate importance.

It is quite clear that under no circumstances can any professional audit be regarded as so complete a safeguard as

to constitute, in effect, an "insurance" against fraud, and it has been expressly held by the Court of Appeal that an Auditor "is *not* an insurer." There is, however, a very vast difference between holding an Auditor liable as an insurer, and expecting him to provide such reasonable safeguards as will, under all normal circumstances, preserve the undertaking against loss owing to dishonesty. Dealing with the matter first of all from the purely commercial—and therefore from the lowest possible—standpoint, the minimum premium charged by an insurance company for a guarantee of honesty is 10s. per cent., and a higher premium is almost invariably charged in the case of employees. A comparison of this figure with most audit fees will show that, if any credit at all is to be given for the actual work of examining the accounts (which work is, of course, never performed by a guarantee insurance company), little, if anything, remains to cover an "insurance" of the honesty of the staff; while a slightly broader—and therefore more common-sense—view of the situation must, of course, show that the risks which insurance companies, with their large paid-up and still larger uncalled capitals, can afford to run in the ordinary course of their business are far different from the risks that any individual professional man could prudently accept. Thus, on the grounds of law, equity, and expediency alike, it is clear that an Auditor does not guarantee his client against all loss by dishonesty. This, however, is, it need perhaps hardly be pointed out, a very different thing indeed from an entire disclaimer of all pecuniary responsibility. The mere fact of an Auditor attaching his signature to the accounts of an undertaking, *quâ* Auditor, is a distinct "representation" to all whom it may concern that the accounts in question have been audited by him; and all, therefore, who are entitled to rely upon this representation are clearly entitled to the assurance (using the word in its popular sense) that the work alleged to have been performed has been conducted with a reasonable amount of skill and care. The exact effect of this "assurance" in each separate case must, of course, be determined upon the

merits of that case; but the safeguard afforded by this personal responsibility of the Auditor is, in itself, by no means a negligible quantity. Further, it may be pointed out that, in the case of professional Auditors, whose living depends upon their reputation for skill and care, a far greater measure of security is provided than the mere legal limit of the responsibility of the Auditor. For obvious reasons it would be inexpedient to strain this legal responsibility too far, or the effect would inevitably be to drive men of substance out of the profession; the chief safeguard of a professional audit, and its great superiority over an amateur audit, lies thus not in any increased measure of legal responsibility (for the law recognises no distinction between professionals and amateurs), but in the safeguard afforded by the fact that the professional depends for his livelihood on his business reputation as a careful and skilful Auditor, whereas the amateur obviously does not. At the same time the efforts that have been made in some quarters to reduce the legal responsibilities of Auditors to "vanishing point" cannot be too strongly deprecated.

OFFICIAL AUDITORS are a class that need not be considered here at any great length—the author's sole object being to produce a work of practical utility to the profession.

Official Auditors are employed to audit the accounts of all local authorities, with the exception of municipal corporations, but the general lines followed in these audits appear to be entirely different to what would be ordinarily understood by that term. As has been already stated, the object of an audit properly so-called, is primarily to detect technical errors and errors of principle in the preparation of accounts, and to discover fraud, either in connection with the accounts themselves or in the handling of the money belonging to the undertaking. It is only indirectly (where at all) that it becomes the Auditor's duty to consider in detail the legality of the acts of those responsible for the conduct of the business. Official Auditors are, however, almost invariably barristers, and the most important part of their duty appears to be to scrutinise the

various transactions, with a view to seeing that they are not *ultrâ vires*. This is, of course, a very important matter in connection with local authorities, but it is to be regretted that the attention of official Auditors should be—as in point of fact it is—almost entirely restricted to a scrutiny of the accounts from this point of view, with the result that, although the accounts are supposed to be checked with a view to detecting error and fraud, it has frequently transpired that dishonesty has remained undiscovered for a very considerable period, and that the accounts themselves are grossly inaccurate in essential particulars. It is suggested that, for the accounts of local authorities to be really effectively audited, the investigation of the official Auditors, with their legal training, should be confined to a scrutiny of the various transactions from this point of view, the actual checking of the accounts themselves being performed by professional Auditors, who by their training are far better qualified than any lawyer to detect both errors in bookkeeping and dishonesty on the part of those having the handling of money. This, it is thought, is the true solution of the difficulty; but, because these matters are always settled on party lines, and never on their merits, it is not likely to be adopted.

THE AUDITOR'S QUALIFICATIONS.—Upon this point a considerable quantity of professional literature already exists. The subject has been touched upon in almost every presidential address delivered since the foundation of the Institute and its various local offshoots. It is not, therefore, proposed to consider the subject at any great length (for, there being no essential difference of opinion upon the matter, such a course appears to be uncalled for), but rather to briefly indicate the qualities that go to make an efficient and a successful Auditor.

FIRST, then, it is very generally conceded that an exhaustive knowledge of every department of bookkeeping is the very “A B C” of the Auditor’s art.

SECOND in importance, probably, is a thorough acquaintance with various statutes regulating the different undertakings in which the Auditor may be concerned.

THIRDLY, although this point has been bitterly contested by some, a sufficient knowledge, not only of business generally, but of the especial way in which various particular businesses are conducted. In his presidential address at the first provincial meeting of the Institute of Chartered Accountants (in October 1886) Mr. FREDERICK WHINNEY, F.C.A., clearly advocated this doctrine when he said: "No Accountant can successfully carry on his practice in all the above-mentioned branches unless he is a person of considerable knowledge, skill, and experience, for he must be not only acquainted with bookkeeping, which is to him as the alphabet only; but, to put it very briefly, he must have some general knowledge of various trades and their customs . . . He ought also to have some knowledge of the practice of the Stock Exchange," and so on. No unprejudiced person would deny the advantage of such a knowledge as is here advocated; the only question being whether the standard set is so high as to be virtually unattainable, and, consequently, impracticable. The reply to this is that, in accountancy, as elsewhere, it is only he who aims at absolute perfection who can expect to attain even to a decent mediocrity. A complete knowledge of everything is not readily attained in three-score years and ten, and is not to be expected as the result of five years' study under articles; but the author never yet heard it seriously suggested that the standard set for the Final Examination of the Institute indicated the limit of desirable or useful knowledge. Only let the Accountant make the most of his opportunities—and he will find that liquidations and bankruptcies, as well as audits, will afford him many—and he will be surprised at the amount of knowledge he can acquire, even in a short time, and perhaps even more astonished at the vast amount of service such knowledge will be to him in his profession.

LASTLY, but not least, may be placed those desirable qualifications of the Auditor which are not acquired by careful study, but, rather, by *living*. Tact, caution, firmness, fairness, good temper, courage, integrity, discretion, industry, judgment, patience, clear-headedness, and reliability. In short, all those qualities that go to make a good business man contribute to the making of a good Accountant; while that judicious and liberal education which is involved in the single word "culture" is most essential for all who would excel. Accountancy is a profession calling for a width and variety of knowledge to which no man has yet set the limit; the foremost Accountants are not ashamed to say that, like Epaminondas, they "learn something in addition every day"; let us, therefore, see no shame in following their example.

AUDIT CLERKS.—It will not be amiss, before leaving this subject, to consider, very briefly, the desirable qualifications of an audit clerk. Conscientiousness may be placed in the foremost rank. A large amount of uninteresting detail must inevitably form a part of the clerk's daily routine; and the fact that the greater portion of such work may generally be scamped, without any great danger of detection, affords considerable temptation, both to the naturally slow worker, and to the gentleman of elastic conscience who wishes to make a little time for himself. Reliability is the first requisite in a clerk, and the clerk who wishes to get on must endeavour to earn a reputation for being "safe." Next, the clerk would be wise—especially the young clerk—not to get too friendly with his client's staff. Let him be cautious of accepting favours, and *most* cautious of accepting presents—which might easily drift into bribes. In this respect clerks may sometimes find themselves in a very difficult position (more perhaps from force of circumstances than from weakness of character), and the possibility of such an occurrence adds another reason to those mentioned in the first chapter, to the desirability of occasionally changing the rounds of the audit clerks. Imagination (under proper control) is another very desirable quality in a clerk;

for, without it, he is apt to become a mere machine, and consequently absolutely useless to the Auditor.

THE AUDITOR'S POSITION.—The position of the Auditor varies to a certain extent with the nature of his appointment, and it will therefore be well to consider the circumstances separately.

THE AUDITOR TO AN INDIVIDUAL will, in almost every instance, receive his appointment from such individual in person; the appointment being—in the absence of stipulation to the contrary—for the period covered by the Revenue Account, but renewable upon the same terms for each successive period, unless a contrary arrangement be made. The fee for the first audit is sometimes settled beforehand, but more usually left open until the time occupied has been ascertained, the fee for subsequent audits being usually arranged after the completion of the first audit. Naturally, the fee charged will be a matter of arrangement; but, in the event of no definite sum having been settled, the Auditor would—in a case of disagreement—be entitled to such sum as a jury would award, which would probably be the usual professional charges. There would be no especial limit to the responsibilities of an Auditor to a sole trader or manufacturer; if he certify a set of accounts as correct, any third party (*e.g.*, a bank advancing money) relying upon his certificate would probably have exactly the same right to expect the accounts to be accurate as though the audit had been performed in pursuit of their own instructions. This is a point that should not be lost sight of, as one is very apt to rely upon the unsupported word of one's own client. At the same time, there is no reason why partial audits (the results of which are *not* certified) should not be made in the case of individuals or firms, provided there is a clear understanding between the client and the Auditor as to the extent of the latter's examination. An Auditor may resign his office at any time, but it is doubtful whether he could then claim to be paid for the time occupied upon an uncompleted audit. On the other hand,

the client may at any time discharge his Auditor, but he would probably be held liable for the whole fee of the current period, if the audit had been actually commenced.

THE AUDITOR TO A FIRM is usually appointed by the mutual agreement of the partners; but, occasionally, by the articles of partnership themselves, or by one particular partner. If appointed Auditor *to the firm*, he must, however, in every case, consider *each* partner as his client, and protect the interests of each accordingly. The same conditions as to terms of agreement, responsibility, fees, and resignation, obtain to the auditorship of firms as were mentioned in the preceding paragraph; but it would seem that any one partner would have power to bind the firm as to the amount of the fees—except, perhaps, where the appointment lay in the hands of one partner, when the consent of such partner would apparently be required. Probably no one partner could discharge an Auditor without the consent of all his co-partners.

This seems the proper place to point out that in practice it not infrequently happens that the letter, if not the spirit, of partnership agreements is broken from time to time; and, so far as these infractions of the agreement relate to accounts, it is clearly the duty of the firm's Auditor to draw attention to the position of affairs in his report. The most usual irregularity of this description is for one or more of the partners to exceed the amount which they are entitled to draw on account of profits; and, although this overdrawing need not necessarily imply bad faith upon the part of the partner concerned, it is important for the Auditor to draw attention thereto, if only for the sake of equitably adjusting the respective interests of the partners. Even where the partnership articles do not provide for interest upon either capital or drawings, it would be well to point out that, as a matter of equity, it is desirable that interest should be charged upon any excess of drawings over the authorised amount, inasmuch as these are clearly in the nature of a loan from the firm to the individual partner, and should, therefore—as a matter of right—carry interest in

exactly the same way, as the law provides that loans from the partners to the firm shall carry interest at the rate of 5 per cent. in the absence of express stipulation to the contrary. Any irregularities of this description should therefore be reported to all the partners ; and, as a matter of convenience, it would appear to be desirable that such report should precede the actual closing of the accounts, so that the instructions of the firm may be taken upon the point and given effect to before the audit is completed. It is very desirable for the Auditor to see that the accounts, after being finally agreed to, are signed by all the partners.

THE AUDITOR ON BEHALF OF CREDITORS.—

It not infrequently occurs that a retiring partner, who leaves a portion of his capital in the firm, or a creditor who makes an advance to a firm, stipulates that " Mr. So-and-so shall audit the accounts." Unless the contrary intention be very clearly expressed, the Auditor so appointed would act on behalf of both the firm and the creditor. In such a case it is very desirable that the amount of the fee be arranged beforehand, and it would not be wise to leave it an open question as to who was to pay it. Under the circumstances the firm could not, of course, remove the Auditor without the consent of the creditor ; nor, in the absence of a special provision to that effect, could the creditor do so, and in any case he would probably be obliged to indemnify the firm against any extra expense occasioned by his so doing. The position of the Auditor, in such a case as this, closely resembles that of the Company Auditor, except that the creditor would be entitled to the fullest possible information, while it is sometimes a question as to whether shareholders have an equally extensive right.

AUDITORS UNDER THE COMPANIES Act 1900.—The Companies Act 1900 has effected several material modifications in the duties and position of the Auditors of all companies registered under the Companies Act 1862 and the various amendments thereof. So far as the Auditor is concerned his position

with regard to the audit of the periodical accounts is identical, whether or not the company was registered prior to the 1st of January 1901. Certain new duties are, however, imposed upon him in connection with issues of shares by companies registered since that date. In Appendix "A" will be found extracts from the Act which call for the special attention of the Auditor. Upon reference to Section 12 it will be noted that every company limited by shares and registered after the commencement of the Act is required to hold a statutory meeting not less than one month, nor more than three months, after the date on which it is entitled to commence business, and that at least seven days before the day on which that meeting is held the directors are required to forward to every member of the company a report containing certain particulars in connection with the issue of Capital and other matters. It is further provided by Sub-section 3 that, in so far as this report relates to the shares allotted by the company, and to the cash received in respect of such shares, and to the receipts and payments of the company on Capital Account, it shall be certified as correct by the Auditors of the company (if any). A new duty is thus thrown upon Company Auditors. Hitherto their responsibility has been confined to the verification of the periodical Balance Sheets, but under the 1900 Act it is provided that if Auditors have been appointed before the statutory meeting they shall certify as correct the various figures which the directors are required to place before the shareholders in advance of that meeting. The *London Gazette* of the 1st of January 1901 contains the forms of the various certificates and returns required under the 1900 Act, and these—in so far as they refer to Auditors—are included in Appendix "A."

It will be seen that Form No. 46 requires the total number of shares allotted to be stated, distinguishing between those which have been allotted for cash and for consideration other than cash, and stating the amount that has been paid up in cash on the former. Separate totals have also to be shown of the amount received by the company in respect of shares issued partly for

cash, and an abstract of the receipts and payments of the company "on Capital Account" to the date of this report must also be given. The form gives no indication as to the precise nature of the required contents, and upon this point some discussion has already arisen among practitioners. The late Mr. A. A. JAMES, F.C.A. (while President of the Institute of Chartered Accountants), expressed the view that as the capital of a company is its *share* capital—and that only—only moneys received on account of shares ought to be included upon the debit side of this account. It would appear that nothing further need be included in order to literally comply with the terms of the Act. In the case, however, of a company making an issue of debentures simultaneously with an issue of shares, it seems clearly desirable that the corresponding particulars with regard to the moneys received on account of debentures should also be given, and this view is advocated by Mr. F. W. PIXLEY, F.C.A., Mr. DANIEL HILL, F.C.A., and others. There can, it is thought, be little doubt that what was intended by the Legislature was that some account upon the lines of the "Capital Account" of Parliamentary Companies kept upon the Double Account System should be provided to shareholders at an early date in order to enable them to see exactly what capital had been raised, what expenditure had been incurred upon Capital Account, and what working capital remained over for the purposes of the company's business. It cannot, of course, be seriously contended that, if this really was the intention of the Legislature, it has been duly provided for in the terms of the Act; but it seems not unreasonable to assume that the prescribed form of account was intended to serve some useful purpose, and it is upon this assumption that the guess has been hazarded that what was required was an account of the Capital Receipts and Payments, such as is ordinarily compiled by an undertaking whose accounts are modelled upon the Double Account System. Apart, however, from the contention of Mr. JAMES, that the proceeds of debenture issues ought not to be included (which, if acted upon, would effectually destroy the utility of the account for the purposes just indicated), it may be pointed out that in any event the prescribed

account is expressly limited to receipts and payments, which (using the words in their ordinary sense, and in the sense in which they are interpreted by the Registrar of Joint Stock Companies) requires all dealings in connection with shares issued as fully paid—and *pro tanto* in connection with shares issued as partly-paid up—to be eliminated altogether. The result is that under no circumstances can the account serve any useful purpose; and, that being so, the precise form in which it is prepared seems comparatively unimportant. It is thought, however, that those undertakings which are desirous of giving the fullest possible information to their shareholders will frame their account upon the lines already indicated, distinguishing, of course, between the pure cash items and the "paper" items—a distinction which can readily be accomplished by the employment of some such form as the following:—

Particulars of Receipts	Cash	Shares	Particulars of Payments	Cash	Shares
	£ s d	£ s d		£ s d	£ s d
Amount received on Allotment of 50,000 Shares of £1 each, 10s. called up ..	25,000 0 0		Amount of purchase consideration ..	25,000 0 0	75,000 0 0
Amount received on issue of £20,000 Debentures at 10s. ..	21,000 0 0		Preliminary Expenses (payment on account) ..	1,200 0 0	
Amount credited as paid on 75,000 Shares of £1 each, issued as fully paid up ..	..	75,000 0 0			
	<u>£46,000 0 0</u>	<u>£75,000 0 0</u>		<u>£26,200 0 0</u>	<u>£75,000 0 0</u>

To make the accounts complete, it is suggested that Preliminary Expenses (if paid) should be included upon the credit side of the account. This, however, can hardly be regarded as essential, in that Form 46 requires a separate estimate to be given of the Preliminary Expenses, whether paid or unpaid, so that this information must in every case be available. The account of receipts and payments should not be balanced, but merely added up, the total receipts and total payments being clearly shown. The objection to showing a balance on this account is

that it would *primâ facie* imply that such a balance existed as cash in hand, whereas, of course, by the date of the report considerable payments will probably have been made on account of revenue.

The prescribed form of Auditor's Certificate to these returns is as follows:—"We hereby certify that so much of this report as relates to the shares allotted by the company, and to the cash received in respect of such shares, and to the receipts and payments of the company on Capital Account is correct." No difficulty ought to arise in connection with this certificate, which is a pure certification of *facts*, whereas, of course, the ordinary Auditors' Report upon accounts is to a large extent merely the expression of a mature and expert opinion.

Passing on to the Auditor's duty in connection with the annual or other periodical accounts; this, so far as it is modified by the new Act, is contained in Section 23 (*vide* Appendix "A"). Some doubt having arisen as to the exact meaning of these provisions, the Council of the Institute of Chartered Accountants submitted a case for the joint opinion of Mr. R. B. HALDANE, K.C., M.P., Mr. C. SWINFEN EADY, K.C. (now Mr. Justice SWINFEN EADY), Mr. A. R. KIRBY, and Mr. F. B. PALMER. The opinion given by these gentlemen is as follows:—

(1) In our opinion the provisions contained in Sections 21, 22, and 23 of the Companies Act 1900 are supplemental to and not in substitution for provisions as to audit contained in the Companies Act 1879 (where applicable), and in articles of association or regulations of a company, and, accordingly, we are of opinion that the Act of 1900 does not relieve an Auditor from the necessity of complying with such provisions, even though the latter impose obligations beyond those imposed by the Act of 1900. In so far, however, as the Act of 1900 is inconsistent with the earlier provisions, the Act must, of course, prevail.

(2) In our opinion the words "books of the company" in Section 23, which give to the Auditor a right of access at all times to the books and accounts and vouchers of the company, mean all the books—not merely the books of account of the company; the words, therefore, include the Minute Books and Letter Books.

books of the company," do not limit the Auditor's duties to a comparison of the figures. No doubt he has to examine the books, but, as Lord Justice Lindley said in *In re The London and General Bank* (1895, 2 Ch. 683):—"He does not discharge his duty by doing this without inquiry, and without taking any trouble to see that the books themselves show the company's true position. He must take reasonable care to ascertain that they do so."

It is a somewhat remarkable fact that whereas, at the time this opinion was first published, the view seemed to be very generally entertained that the wording of Section 23 was perfectly clear and intelligible, the greatest diversity of opinion has been since expressed with regard to the exact meaning of these provisions, and even now nothing approaching uniformity of view has been arrived at. It is unnecessary here to repeat all the various interpretations that have been placed upon this comparatively simple clause, but in order to deal completely with the subject it is necessary to draw attention to a few of the points upon which most doubt appears to exist. These points are briefly as follow:—

- (a) What are the "requirements" of the Auditor?
- (b) What should be the normal wording of the Certificate appended at the foot of the Balance Sheet?
- (c) How far should the Report be independent of such Certificate?
- (d) How far the provisions of the Act may be modified by special Articles of Association.

With regard to (a), the joint opinion already referred to expresses the view that the word "requirements" must be taken "in its popular sense, and not as referring merely to what the Auditor is entitled to require under the preceding words of the section." It may be questioned, however, whether this throws much light upon the point under discussion. The popular sense of the word "require" cannot by any stretch of imagination be made into anything more general than "to

deliberately ask for, with authority"; and, inasmuch as the only "authority" conferred upon Auditors is that comprised in the preceding words of the section (and in any special Articles that may amplify them), it will be seen that the distinction drawn by learned Counsel is a somewhat narrow one. It would, indeed, seem as though the certification which the Auditor is required to give at the foot of every Balance Sheet, that his requirements as Auditor have been complied with, means nothing more nor less than the certification that he has been afforded all due facilities to be able to make a proper audit of the accounts. It is impossible to give an exhaustive list of what those facilities might be in every case; but it is suggested that, if the books are so incomplete—or have been so inaccurately kept—that the Auditor feels they afford no true index to the actual facts; or if he has been refused access to any of the books, or to any vouchers, documents, or papers that may be required to verify them; or if explanations, properly asked for, are not forthcoming; or if mistakes of fact which he has pointed out have not been corrected; or if the accounts are not prepared in the form prescribed by any Act of Parliament governing the company, or by its own regulations: then it becomes the duty of the Auditor to refuse to certify that all his "requirements" as Auditor have been complied with. It is submitted that in such a case the Certificate should not merely take a negative form, but should state in what respects the Auditor's requirements have not been complied with; but—as suggested by Counsel—if the full explanation be lengthy, the details might with advantage be relegated to the Report.

In particular it may be pointed out that there is a very broad distinction between the proper "requirements" of an Auditor, and that which it may be his duty to represent to the Directors as being a matter for their consideration.

- Passing on to (b), the greatest controversy arises as to whether the Certificate appended to the foot of the Balance Sheet should, or should not, contain anything in addition to

the express requirements of Section 23. In the joint opinion already referred to it is stated that there would be "no objection, if it be desired, to connect the Certificate with the Report by inserting in the Certificate a reference to the 'subjoined' or 'accompanying' Report; or, as an alternative, where thought expedient," the Report might be incorporated with the Certificate. If, however, this course be adopted, it is, Counsel think, "still necessary that the Auditor should make and sign the Report separately, and send it in to the Directors to be placed before the shareholders." This opinion throws very little light upon a point concerning which the greatest diversity of views exists among practitioners. It may be stated at the outset that many, if not most, of the leading practitioners appear to have made it a general practice to issue a combined Certificate and Report at the foot of the Balance Sheet, in some such form as the following:—

"In accordance with the provisions of the Companies Act 1900 we certify that all our requirements as Auditors have been complied with, and we report to the shareholders that we have audited the above Balance Sheet and Profit and Loss Account with the books relating thereto in London, and with the returns received from the foreign and colonial branches. Some of the investments are deposited in connection with business abroad, in accordance with foreign or colonial State laws. In our opinion such Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs, as shown by the books of the company."

It will be seen that such a form as this is upon the same lines as the Auditor's Certificate that would have been given in normal cases *prior* to the 1st January 1901, with the purely formal addition of the statement rendered compulsory by Section 23, that all the requirements of the Auditor have been complied with. Doubtless the directors of most established companies prefer that there should be this continuity of method, and shareholders who are unable (or too lazy) to personally attend the general meetings would also, no doubt, favour the full publication of all that the Auditors might have

to say. It is submitted, however, that the practice—as a general practice—is open to the following serious objections:—

- (1) It undoubtedly suggests that there is nothing in the *unprinted* Auditor's Report that is not also printed at the foot of the Balance Sheet.
- (2) It deprives Directors and Auditors alike of the great convenience afforded them by the Legislature, which provided for the issue of an Auditor's Report that should not necessarily be published.
- (3) In the event of any occasion arising in the future when it becomes important for the Auditor to make a special Report to the shareholders, a very difficult position of affairs arises which (it is submitted) Section 23 was expressly intended to obviate.

With regard to the first point, it may of course be assumed that all persons are supposed to know the law, which provides for the existence of a separate, unprinted, Report that shall be read at the general meeting. It is submitted, however, that those who have led the public to suppose it to be their custom to incorporate their Report in their Certificate cannot with propriety avail themselves of this legal fiction.

With regard to the second point, it seems clear that the intention of the Legislature was to encourage the Auditor to report to the shareholders upon all matters within his province that he thought worthy of their consideration, and to educate them into a more accurate appreciation of the advantages and necessary limitations of an audit, while at the same time encouraging them to take a more active interest in their own affairs. It goes without saying that the disinclination of shareholders to concern themselves with anything beyond the receipt of dividends is one of the most fruitful causes of irregularities of every description in connection with company promotion and administration; and it is equally certain that, without usurping the functions of directors, Auditors might,

by timely advice, frequently prove themselves of the greatest possible use to both directors and shareholders. Whether the provision of a separate Auditor's Report would in practice achieve all these beneficial results, time alone can show; but it seems—to say the least of it—highly desirable that an attempt should be made to give the Act a fair chance, while it is certainly not too much to say that the inevitable result of including the Auditor's Report in the Certificate as a matter of course is to effectually crush all hopes in this direction.

Lastly, no one can foresee the future. An occasion may arise in connection with even the soundest enterprise when the Auditor, in the due discharge of his duties, feels called upon to make some special statement to the shareholders. Prior to the 1900 Act such a statement had, of necessity, to be made upon the face of the Balance Sheet, open to all the world; with the result that the Auditor might, as likely as not, damage the shareholders by his disclosure, instead of serving their interests. In the past, therefore, the position of the Auditor has been one of the very gravest responsibility and difficulty. The statutory provision of a separate Report has entirely removed this difficulty, and also (in a great measure) the responsibility; yet it seems obvious that the Auditor who has systematically ignored the opportunities afforded by Section 23, year after year, cannot with propriety suddenly alter his practice in a moment of danger, and then—and then only—issue a confidential Report to shareholders which will come before them only at the general meeting. It is thought that any Auditor who adopted such a course would be placing himself in a position of very considerable personal danger, and for this reason—if for none other—the author would wish to emphasise as strongly as possible the advantage of making it a *general practice* to issue a Report separate from the Certificate at the foot of the Balance Sheet.

It is thought that this view of the position of affairs is becoming increasingly apparent among auditors, although (as has been already stated) it finds but scant encouragement

among the leading practitioners. Mr. F. W. PIXLEY, F.C.A., has, however, very strongly expressed himself in favour of the separate Report being issued in every case, and among others who have expressed themselves to the like effect Mr. H. W. KIRBY, F.C.A., may be named: *per contra* the practice appears to find little favour with such firms as COOPER BROS. & Co.; PRICE, WATERHOUSE & Co.; DELOITTE, PLENDER, GRIFFITHS & Co., and others of first-class reputation.

(c) If the Report be incorporated in the Certificate, the wording of the latter must of necessity be sufficiently wide to embrace all that appears in the former, but to literally comply with the terms of Section 23 it is necessary (as the joint opinion of Counsel points out) that a Report should still be forwarded to the Directors, to be read at the general meeting. If, however, the practice—which it is thought is greatly preferable—be adopted, of keeping the Report distinct from the Certificate in all cases, the question arises as to what the wording of the latter should be. Mr. PIXLEY has expressed the view that the Certificate should contain such particulars and information as the Company's Articles of Association may prescribe. It is thought, however, that this statement is founded upon a misapprehension. All ordinary Articles of Association refer to an Auditor's *Report*, but not to an Auditor's *Certificate*; and whatever, therefore, the Articles of Association may require the Auditors to "report to the shareholders" should, it is submitted, be included in the Auditor's Report, and not necessarily in the Certificate appended at the foot of the Balance Sheet. Indeed, if anything of a detailed nature be included in the Certificate, there is—at all events as matters now stand—serious danger that shareholders will consider that the Certificate includes the *whole* of the Report. There is, therefore, every argument in favour of the wording of the Certificate being kept as bald as possible, so as to draw prominent attention to the existence of a *separate* Report.

Mr. PIXLEY has stated ("Duties of Auditors," 9th edition, p. 445) that the statutory "requirements" of Auditors include (*inter alia*):—

“(d) The full allowance for depreciation of wasting assets, or for loss likely to arise on realisation of debts.

“(e) The setting out in full and ample form the statements the Auditor is desired to sign.”

It seems very doubtful whether these assertions can be sustained. With regard to (d), it has been shown elsewhere that the Legislature and the Courts, in their mutual desire to avoid placing unreasonable demands upon Directors, have studiously refrained from insisting upon a due provision for depreciation, even in the case of admittedly “wasting” assets, and there is no ground for supposing that the Auditor is possessed of any higher authority. Perhaps this is to be regretted; but surely nothing is to be gained by an assumption of power that is not backed by the requisite authority. Moreover, it may well be doubted whether the Auditor is, by virtue of his training, competent to express a better or more reliable opinion on the subject of depreciation than the Directors, who may naturally be supposed to be experts in the class of business transacted by the company. On the other hand, if the Auditor, in all seriousness, honestly does not believe the accounts to be “full and fair,” obviously he cannot undertake to *report* to the shareholders that they are. With regard to (e), this seems to be entirely a matter for the Auditor’s Report: there are no grounds for suggesting that he is entitled, as of right, to deal with the matter in his Certificate, unless the accounts are so inadequate as to be fraudulent. The accounts submitted to the Auditor are the accounts of the Directors, with whom the main (if not the only) responsibility rests. It is for the Auditor to examine and report to the shareholders on these accounts; but there is nothing in the Companies Acts to suggest that he has any power to require the Directors to amend them in any way. This may be very regrettable, but that is another matter altogether.

There is nothing whatever to prevent the Auditor’s Report being printed along with the Balance Sheet, if the Directors so wish; but there is the greatest possible objection to a

Certificate, which, in effect, amounts to a Report, being printed alone, if no notification appears upon the face of it of the existence of a separate Report, although there is nothing in the 1900 Act to require such a reference to be made.

The following appears to be a good form of certification, which possesses the further advantage that it requires no modification, even if the Report should contain something unusual :—

“ In accordance with Section 23 of the Companies Act 1900, we hereby certify that we have audited the accounts of the ————— Company, Lim., and reported to the shareholders thereon under this date. We further certify that all our requirements as Auditors have been complied with.”

(d) It now only remains to consider the effect that special Articles of Association may have upon the general position of affairs. The 1900 Act, of course, takes precedence over the Articles where the two conflict, but any provision contained in the Articles that is not inconsistent with the terms of the Act must be complied with. It has already been pointed out, however, that in all ordinary cases these provisions would not require any modification in the wording of the Certificate: it is moreover submitted that, where the Articles of Association do prescribe that additional information as to the position of affairs shall be contained in the Certificate, they are now inoperative, as being contrary to the spirit of Section 23. For the same reason it is thought that a clause providing that any Report on the accounts issued by the Auditor shall be printed along with the accounts no longer applies, the Act of 1900 having expressly provided a means by which the Auditor may properly communicate with the shareholders *without* the necessity of his communication being published broadcast.

OTHER POINTS.—Under the Companies Act 1900 the first Auditor may be appointed by the Directors at any time prior to the statutory meeting. Any Auditor so appointed, however, vacates office at the first annual general meeting; it

devolves upon the shareholders to fill the vacancy so caused, either by re-electing the retiring Auditor or by appointing another in his stead. If no appointment be made by the shareholders at the meeting, there is apparently a "casual vacancy" in the office which may be filled by the Directors; under Section 21 (2), however, the Board of Trade *may* appoint an Auditor under these circumstances. The Directors may also fill any vacancy caused by the retirement or death of an Auditor. When the appointment is made by the Directors they fix the remuneration, but if the Company in general meeting makes the appointment it fixes the remuneration, while the Board of Trade has the like power if it makes an appointment under Section 21 (2). If, however, the shareholders omit to fix the Auditor's remuneration, he must wait until another general meeting has been called and a resolution regularly passed, as the Directors have no power to fix the remuneration of an Auditor whom they have not appointed.

The above remarks apply in their entirety only to the Auditors of companies coming under the scope of the Act of 1900. This Act does not apply to companies formed under special Act of Parliament, Deed of Settlement, &c., nor to companies registered abroad (including the Isle of Man and the Channel Islands). The position of the Auditors of such companies has therefore still to be considered.

THE AUDITOR OF COMPANIES other than those registered under the Companies Acts 1862 to 1900 is subject to the rules and regulations of the company concerned, and to such further statutory provisions as may apply to the particular class of undertaking. The usual practice is for him to be appointed, in the case of a new company, by the Directors; but he is subject to re-election at each successive general meeting, or occasionally at each alternate meeting, and at any such meeting the shareholders may (theoretically), if they so please, appoint another Auditor. Unless the remuneration of the Auditor is fixed at the time of his appointment, or by the

articles of association, he is entitled to a reasonable remuneration; but if appointed "at such remuneration as the shareholders may think fit," he is entitled to such sum as the general meeting may award him—and no more. Directors have no power to dismiss an Auditor, once appointed; but, apparently, an Auditor may resign at any time, although probably at the loss of his fees for the uncompleted work. A casual vacancy can be filled by an appointment at an extraordinary general meeting, but many articles of association give the Directors power to fill a casual vacancy.

A resolution appointing "A. B. & Co." Auditors of the company in effect appoints all the then partners in the firm "A. B. & Co." In the event of one (or more) partners retiring it is thought that the appointment would rest with those who, being partners at the date of the resolution of appointment, are entitled to the use of the firm name.

To a great extent it rests with the Directors to decide how much information shall be supplied in the published accounts, but the Auditor must not lose sight of his individual responsibility. He should be particularly careful to guard against juggling with words, and so appearing to give a full Certificate, when in reality he is "making himself safe," or "hedging" behind a Certificate which, when carefully analysed (and only then), is found to be most qualified. He must, in every case, be satisfied in his own mind that the accounts are correct, and fairly stated.

It has been settled by the Court of Appeal, in the *Kingston Cotton Mills* case, that the Auditor of a company appointed under a normal set of articles of association is an "officer" of that company, and the same Court in the *Western Counties Steam Bakeries* case decided that the Auditor is *not* an "officer" of a company within the meaning of the Companies Act 1890, even if he has performed the duties of an Auditor and held himself out as such, if in point of fact his appointment has been irregular, and not in accordance with the regulations of that particular company.

At one time the view was very generally entertained in the legal profession that the decision of the Court of Appeal in the *Kingston Cotton Mills* case, just referred to, was unsound, and that, had this case gone to the House of Lords, it would have been reversed. In this connection it is perhaps of interest to note that an appeal to the House of Lords was entered; but not proceeded with, because in the meantime the case was set down and heard upon its merits. It is thought, however, that the tendency of the present day is unquestionably in favour of the Auditor of a company being regarded as an officer of that company, and whatever technical objections might be raised against this view it certainly seems to be supported by common sense. Although, therefore, the question cannot be regarded as altogether free from doubt, it would seem to be reasonable to assume that, as matters now stand, the Auditor of every joint-stock undertaking is an "officer" of that undertaking. This view would certainly seem to be supported by the Companies Act 1900, which provides for the appointment of an Auditor in connection with every company, thus making an Auditor an indispensable part of what may be called its equipment.

RESIGNATION OF AUDITORS.—There is nothing whatever in connection with this subject in the Companies Acts 1862-1900. Any right that the Auditor may have to resign is therefore entirely founded upon custom. It is not for a moment disputed that an Auditor would at any time have a right to resign his position, and were he to do so the "casual vacancy" which is referred to in both the Acts would, of course, arise; but it is surprising that the matter should not be dealt with more explicitly.

A point of considerable interest to all Accountants is the question as to what an Auditor ought to do when he finds himself in hopeless disagreement with the Directors upon a question as to what ought to be done in the way of treating certain items in the company's accounts. Only too frequently the course adopted is for the Auditor to resign, so that the Directors can

fill up the casual vacancy thus caused by appointing someone who happens to agree with their own view, and so the whole matter is hushed up, and never comes to the knowledge of the shareholders at all. So long as matters remain upon the present footing, no one can possibly blame any Auditor who prefers this means of escaping a possible liability ; but, on the other hand, it is obvious that this procedure effectually detracts from the independence of an audit. If there is any advantage at all in having an Auditor, independent of the management, to supervise the accounts of a company, it is that, in the event of his discovering anything which he thinks should come to the knowledge of the shareholders, then that something will be placed before them. Under existing circumstances it is probably not once in ten times that an occurrence of this kind is ever found out by the shareholders. All that they know is that the accounts have been audited. They have probably quite forgotten the name of the previous Auditor, and no intimation is made to them of the fact that a change has occurred. This is a state of affairs which, so long as it continues, will effectually prevent any practical effect being given to the reforms which the Act of 1900 appears to be desirous of aiming at.

The only way of getting rid of the difficulty appears to be to provide that an Auditor, when once appointed, should remain in office until removed by a special resolution of the shareholders in general meeting, or by the Board of Trade ; or, should this be thought too drastic, then it might be provided that the Auditor remains in office for a term of, say, three or five years, which, no doubt, in the majority of cases would render the Auditor independent of every whim of the Directors. As matters stand at present, it is not exaggerating the case to say that, while the Legislature is straining every nerve to throw increased responsibilities upon Auditors, no effort whatever has been made to make it possible for them to effectively discharge the duties which are being cast upon them, without at the same time incurring serious personal responsibility.

“PRIVILEGE” OF AUDITORS.—Another reform in this connection which is earnestly needed is absolute “privilege” upon the part of an Auditor in his Reports. To a certain extent he, no doubt, has this privilege at the present time; but the point is not free from doubt, and it should be absolutely clear. If the Auditor is of the opinion that something which has been done by the Directors, or by any outside persons, calls for the attention of the shareholders, he should be in such a position that he need feel no hesitation in expressing his view. He ought also to have a much more clearly defined right to circularise the shareholders, if need be, at any time; and more particularly, in the event of his having resigned, as to the reasons for his resignation. It will, of course, be said that, were this done, many sound companies and many honest Boards of Directors would be placed at the mercy of unscrupulous Auditors; but there is at least no more harm in a company being at the mercy of unscrupulous Auditors than in its being at the mercy of unscrupulous Directors, and unquestionably the latter are more common than the former. Besides, the Auditor would always be liable to be called upon to justify the position which he had taken up; and nothing could protect him in the way of “privilege,” if it could be shown that he had not been actuated by motives of good faith.

REMOVAL OF AUDITORS.—Passing on to the question of the removal of an Auditor. This can only be done by the company at its annual general meeting—that is to say, the only practical way of removing an Auditor is not to re-elect him when his year of office has expired. As, however, most companies only require the services of their Auditors immediately *before* such annual meeting, this for all practical purposes amounts to an appointment at will; and, in view of the fact that, under any but the most abnormal circumstances, the Directors of a company can always secure a majority at a poll, it will be seen that the Auditor (as matters now stand) practically holds his appointment from the

Directors, even although he may not do so in form. It is for this reason that some sort of security to the Auditor for the tenure of his office has been so strongly advocated.

DUTIES OF AUDITORS.—With regard to the question of the duties of an Auditor while in office. There being, up to the present at all events, no very definite provisions in the Companies Acts with regard to this matter, the question is largely one of contract between each individual Auditor and the company. The basis of that contract will be construed by the Courts chiefly from the articles of association regulating that company. Table "A" deals with this subject in Articles 92 to 94, and it may be stated that most articles of association follow very closely upon these lines, although very often the question is dealt with very much more shortly. Section 23 of the Companies Act 1900, however, of course governs the matter so far as it goes.

In this connection it may be pointed out in passing that, even with regard to such important questions as the value of assets, provision for depreciation, the assessment of profits earned, and the distribution of unrealised profits, the Courts have shown a marvellous disinclination to lay down any general rules which could be regarded as principles for the safe guidance of Auditors in the future. In carefully and laboriously shirking their duties in this respect, however, the Courts have been most ably seconded by the Legislature, which has been particularly cautious in abstaining from laying down any exact rules as to what the duties of an Auditor may be. No doubt it has acted wisely in adopting this course, however, because any attempt to state explicitly what the duties of Auditors are in all cases would inevitably fail in not a few, and would afford the best possible excuse for the insufficiency of the audit that had been performed in such cases. Any Act of Parliament which attempts to classify the duties of an Auditor under stereotyped headings must at least profess to be at the same time exhaustive, and as the latter

is impossible it seems to follow that the former is very inexpedient.

RIGHTS OF AUDITORS.—The rights of a Company Auditor may be very shortly dismissed. He has but few. He has the right to hold office till the next general meeting of the Company—which is of but little use, seeing how easily Directors may make things impossible for him in the meantime, and how naturally disinclined any professional man would be to be removed at a public meeting. He has also the right to a remuneration at such a rate as the Directors or the Company in general meeting may be pleased to allow. He has the right to examine the books and accounts of the company at all reasonable times (which, unless coupled with a reasonable scale of remuneration, is, perhaps, rather more of a curse than a blessing), and he has the further right of making any inquiries from “Directors or other officers of the company” as to matters which may not appear to be clear to him from an inspection of the books and documents. As it has been decided that neither the solicitors nor the bankers of a company are “officers of the company,” it will readily be seen that two most important sources from which the Auditor must necessarily require information under most circumstances are not legally open to him.

OTHER CONDITIONS govern the appointment of Auditors under various general and special Acts of Parliament, but these may be readily gathered from a perusal of the particular Acts involved, and—as the differences are, for the most part, formal—need not now be entered into.

CHAPTER X.

THE LIABILITIES OF AUDITORS.

THE LIABILITIES OF AUDITORS.—Turning now, again, to the general aspect of the question, it will be well to consider the extent of the Auditor's liability in connection with accounts that he has certified.

The question appears to be capable of division under two heads, viz.:—

- (1) What is the actual extent of the Auditor's certification ?
- (2) What is his legal responsibility in case of an error being subsequently discovered in accounts that have been passed by him ?

To take these two points separately.

THE EXTENT OF AN AUDITOR'S CERTIFICATION.—Unfortunately, this is a matter upon which the profession is by no means agreed ; while, on the other hand, the cases that have been decided by the Courts are so few, and the questions actually at issue so narrow, that sufficient precedents are not even yet available to definitely settle the matter. At the same time, it is well to remember that, however desirable it may be to know exactly the bare extent of the legal responsibility, the real professional responsibility to clients ought always to be the ideal ; and, further, an Auditor will be the worst of friends to his profession if he studiously exert himself to narrow the responsibilities, and so to dwarf the importance of his position.

The responsibility involved in certifying a Balance Sheet to be absolutely correct would be so great, so limitless, that many have preferred to discard all claim to such a position of certainty, and prefer merely to certify a Balance Sheet as being "in accordance with the books." Auditors, however, will hardly require to be reminded that an investigation which had been limited to the comparison of a Balance Sheet with the books would be, for every purpose, absolutely valueless. So obvious is this conclusion that no professional Auditor would ever think of confining his investigation to this particular point, yet many experienced Auditors appear to be afraid to make any certification as to the result of such further investigation as they know to be essential. Such a state of affairs is unsatisfactory to the client and discreditable to the Auditor. Again, it is a very open question as to whether so unsatisfactory a certificate would ever have the effect of limiting the legal responsibility of the Auditor to the exact points certified. It is, at least, possible that the Court would view the matter from a broader aspect, and consider that the man who had accepted the position of Auditor—to say nothing of the fees incident thereto—had also undertaken the responsibilities of that position, and that it would be disposed to form its own opinion as to the real extent of such responsibilities. Such, indeed, appears to have been the view taken by STIRLING, J., in the case of *The Leeds Estate, &c., Society*. It would appear, therefore, that the Auditor who does not consider his investigation has been sufficiently searching escapes no liability by issuing a carefully modified certificate; and, indeed, such a course is somewhat dishonest. These are strong words, but not stronger than the circumstances appear to require.

Since the passing of the Companies Act 1900 provision has, however, been made for Auditors (of companies to which the Act applies) to make their qualifications, not at the foot of the published accounts, but in a Report which the Directors are required to have read at the general meeting. This Report may

—and, of course, should be—as lengthy and as detailed as circumstances may require, and there is thus—now, at least—no excuse for cryptic certificates which may mean anything or nothing. It is suggested that the Auditor should so word his annual Reports as to encourage, by every means that lies in his power, an intelligent and active interest on the part of shareholders in the accounts of the company, and in its finances generally.

When addressing the Autumnal Meeting of the Institute of Chartered Accountants in 1888, Mr. FREDERICK WHINNEY, F.C.A., expressed himself as follows: “I know perfectly well that a proper Auditor must go further (than comparing the published accounts with the books) and see that the books themselves do correspond with facts,” and this view appears to be endorsed by the legal decisions to be considered later on. As to how far it is possible for this standard to be carried into practice, there is perhaps some room for the elasticity of individual opinion, but the general statement is absolutely unassailable.

In actual practice, however, the question naturally arises: How is the Auditor to ascertain the actual facts? To which it may be replied: In the same manner as a judge or jury—*by sifting evidence*. The chief evidence is, of course, the books (and it may be remarked incidentally, that it is clearly the Auditor's duty to see that the accounts he certifies, in addition to being correct, *are* in accordance with the books), but the books must not be considered the sole source of evidence; the fact that a statement appears in the books is *prima facie* evidence only, and must be verified, either by internal cross-examination, or by reliable and independent evidence, whether documentary (vouchers, &c.) or oral (explanations).

The result of such an investigation will be that the Auditor has proved to himself that certain statements represent absolutely indisputable facts, and that certain other statements, *in his opinion* appear to represent facts. Beyond this—not being

omniscient—he cannot go, and should never attempt to go. Let him therefore report that he has thoroughly examined the accounts, that they are in accordance with the books, and are, in his opinion, correctly stated: he will then be occupying a logical, manly position—far more in keeping with the dignity of his profession than that afforded by the most skilful of word-juggling. (The Companies Act 1900 has helped to clearly define the limits of an Auditor's responsibility, and proceeds upon the above lines.)

The view laid down in the two preceding paragraphs is that which appeared in the first edition of this work, which was published in 1892, before the London and General Bank had failed, and before the celebrated case in connection with that failure was thought of; but nothing that has since occurred has in any degree tended to discredit the line of argument then taken. On the contrary, the judgment of Lord (then Lord Justice) LINDLEY fully endorses the author's view. This judgment, together with that of the late Lord Justice RIGBY, will be found fully reported in Appendix "B"; but for the sake of clearness, and on account of its extreme importance, it has been thought desirable to reproduce here the following extract from Lord Justice LINDLEY's judgment:

"It is no part of an Auditor's duty to give advice either to directors or shareholders as to what they ought to do. An Auditor has nothing to do with the prudence or imprudence of making loans with or without security. It is nothing to him whether the business of a company is being conducted prudently or imprudently, profitably or unprofitably; it is nothing to him whether dividends are properly or improperly declared, provided he discharges his own duty to the shareholders. His business is to ascertain and state the true financial position of the company at the time of the audit, and his duty is confined to that. But then comes the question: How is he to ascertain such position? The answer is: By examining the books of the company. But he does not discharge his duty by doing this without inquiry and without taking any trouble to see that the books of the company themselves show the company's true position. He must take reasonable care to ascertain that they do. Unless he does this, his duty will be worse than a farce. Assuming the books to be so kept as to show the true position of the

company, the Auditor has to frame* a Balance Sheet showing that position according to the books, and to certify that the Balance Sheet presented is correct in that sense. But his first duty is to examine the books, not merely for the purpose of ascertaining what they do show, but also for the purpose of satisfying himself that they show the true financial position of the company. This is quite in accordance with the decision of Mr. Justice STIRLING in *The Leeds Estate Company v. Shephard*, in 36 Chancery Division, page 802. An Auditor, however, is not bound to do more than exercise reasonable care and skill in making inquiries and investigations. He is not an insurer; he does not guarantee that the books do correctly show the true position of the company's affairs; he does not guarantee that his Balance Sheet is accurate according to the books of the company. If he did he would be responsible for an error on his part, even if he were himself deceived, without any want of reasonable care on his part—say, by the fraudulent concealment of a book from him. His obligation is not so onerous as this.

“ Such I take to be the duty of the Auditor ; *he must be honest—that is, he must not certify what he does not believe to be true, and he must take reasonable care and skill before he believes that what he certifies is true.*

“ What is reasonable care in any particular case must depend upon the circumstances of that case. Where there is nothing to excite suspicion, very little inquiry will be reasonable and sufficient; and in practice, I believe, business men select a few cases at haphazard, see that they are right, and assume that others like them are correct also. Where suspicion is aroused more care is obviously necessary, but still an Auditor is not bound to exercise more than reasonable care and skill, even in a case of suspicion; and he is perfectly justified in acting on the opinion of an expert, where special knowledge is required.

“ Mr. THEOBALD's evidence satisfies me that he took the same view as myself of his duty in investigating the company's books and preparing his Balance Sheet. He did not content himself with making his Balance Sheet from the books without troubling himself about the truth of what they showed. He checked the cash, examined vouchers for payments, saw that the bills and securities entered in the books were correct, took reasonable care to ascertain their value, and in one case obtained a solicitor's opinion on the validity of an equitable charge. I see no trace whatever of any failure by him in the performance of this part of his duty. It is satisfactory to find that the legal standard of duty is not too

* This is clearly a *lapsus lingui*: it is no part of an Auditor's duty to prepare accounts; but to examine and report upon accounts prepared by, or on behalf of, the directors.

high for business purposes, and is recognised as correct by business men."

The reasons why their Lordships felt constrained to give judgment against the defendant, notwithstanding the fact that they could "see no trace whatever of any failure by him in the performance of this part of his duty," will be considered under the following sub-heading.

Since the second edition of this work was published several important decisions with regard to the liability of Auditors have been delivered by the Courts, which—to a certain extent, although still very unsatisfactorily—tend to further define the extent of an Auditor's certification. It is thought that the points raised in these various judgments can be more conveniently dealt with under the heading of the liabilities of Auditors. It may be mentioned here, however, that, in the *Kingston Cotton Mills* case, it was decided by Mr. (now Lord) Justice VAUGHAN WILLIAMS that although the Directors of a company were justified in accepting the certificate of the managing director as to the amount of stock in hand, the Auditors were—at all events in that particular case—not so justified, and that although their certificate was qualified accordingly; but this decision was overruled by the Court of Appeal.

An interesting side-light upon the exact extent of an Auditor's certification is afforded by the proceedings of the Select Committee of the House of Lords appointed in 1896 to inquire into Company Law Amendment, upon the occasion of the examination of Mr. FREDERICK WHINNEY, F.C.A. The following extract from the published report of these proceedings will be found of no little interest, but it is important to remember that, although some of the Law Lords have here expressed themselves in terms that appear to be widely different from those which have from time to time been used by other Judges, they were not speaking *ex cathedra*; and further that, although the distinct suggestion is that, should a case be brought before it, the House of Lords might see fit to overrule

some of the decisions already given by the Court of Appeal, it does not necessarily follow that their Lordships would adhere to those views (as expressed below) when the time came :—

“ Passing to clause 29, which deals with the appointment of Auditors, he suggested the addition of words to the effect that, unless it was otherwise provided by the articles of association, one of the Auditors or the Auditor, if there was only one, should be a professional accountant, and should not necessarily be a shareholder. In support of that proposition, he pointed out that joint-stock enterprise had grown very largely of late years, and he maintained that very few Balance Sheets could be audited properly except by a professional accountant. He went on to suggest the insertion in the Bill of a provision that no Auditor, other than the retiring Auditor, should be appointed at a general meeting, unless notice had been sent out to the shareholders with the notice of meeting. That, he said, was brought forward with the object of preventing the question of the Auditor being ‘rushed,’ as was sometimes the case at present. The Bill provided that there should be a Balance Sheet containing all details—technically, what was known as the Trial Balance. It was scarcely necessary to provide for that by legislation, because a Balance Sheet could not be made out unless the details were given. As to the duties of Auditors, the Bill proposed that they should use reasonable diligence with the view of ascertaining that the books of the company had been properly kept, and recorded correctly the financial and trading transactions of the company. The latter part of the section he did not object to, but he thought the words ‘properly kept’ should be omitted. ‘Properly kept’ was a vague term, and the section would be quite sufficient to meet the difficulty without its insertion. It would be the duty of the Auditors to say that the books had not been properly kept if that was the case.

“ The Bill cast upon Auditors the duty of checking the Balance Sheet, including the amount of debts due to the company after making a proper deduction for debts considered to be bad or doubtful. It would be impossible for the Auditors to do that in the case of large companies, where the debtors numbered, say, 1,000. In the case of banks, for instance, where the number of debtors was very large, it was found necessary to keep an aggregate account of debtors, showing the total amount due to the company by its debtors. The Auditors would have to take that account, and schedules would be prepared, and, if necessary, would be tested afterwards. The duty should not be thrown upon Auditors of checking every balance. In one case he might mention the debtors numbered 750,000. (Laughter.) It should be sufficient if they

gave a certificate to the effect that they had used all reasonable care and diligence in ascertaining that the Balance Sheet was true."

LORD DAVEY: "I should like to ask whether you conceive it to be the proper duty of an Auditor to say not only whether the books are properly kept, but to go into questions behind the books, and say whether the assets are properly valued?"—"I do not know that I can give a better definition of the duties of the Auditor than that laid down by Lord Justice LINDLEY. He said that it was the duty of an Auditor to be honest, to exercise all reasonable care and skill to ascertain that that which he certifies is true, and to exercise all reasonable care and skill in ascertaining the truth."

LORD FARRER: "That is all very well; but what is the truth which he is to ascertain?" LORD DAVEY: Yes; that is it. Can he, for instance, when the properties are valued at a certain sum in the books, and on the face of the books are properly valued, can it be his duty, not being a valuer, to go into the question of value and say that the directors have put too high a value on the real estate?"—"No; I do not think so. It would be giving the Auditor a different position from that which it was contemplated he should have—namely, that he should examine the accounts of the directors and see whether they are correct. Anything calculated to arouse his suspicion he ought, of course, to look into."

LORD FARRER: "After all, the responsibility lies with the directors?"—"Not altogether with the directors. There are the managers of the company."

LORD FARRER: "Do you wish to place the Auditor in the position of an administrator, who is to check the directors in their management of the company?"—"Certainly not."

LORD DAVEY: "Is not the sounder principle this—that the Auditor is bound to know everything the books tell him, to have all the suspicions that the books suggest, and to make all the inferences to what he finds in the books would lead him?"—"I think that would cover the whole of his duty. I think it is his duty not to certify a Balance Sheet until he believes it to be true, and he has taken all reasonable care that it is so. He is bound to see that the Balance Sheet is brought before the shareholders in such a form that they themselves can exercise their judgment upon it."

"The next suggestion he had to make was that the pains and penalties of Auditors should be modified. At present the Auditor was supposed to be responsible if dividends were paid out of capital."—LORD DAVEY: "Is he? I never knew it."—THE LORD CHANCELLOR: "Putting aside

fraudulent connivance, what do you suppose to be the responsibility of an Auditor? "—The witness: "That if dividends have been paid out of capital, assuming, of course, that the company is wound up, the directors and Auditors are responsible for the amount of the dividends so paid, subject to the Statute of Limitations in favour of the Auditors."—Lord DAVEY: "Where do you find that?"—The LORD CHANCELLOR: "I am not aware of any such law. I am not aware of any case in which the innocent mistake of a director has been held to be the subject for an action."—The witness: "There was a case before Mr. Justice STIRLING"—Lord DAVEY: "There, there was fraudulent connivance."—The witness: "I think there was not connivance, but that the Auditor himself was ignorant."—The LORD CHANCELLOR: "To me it is a startling suggestion that for an innocent mistake an Auditor should be liable."

The view expressed by the late LORD DAVEY above was, it will be seen, that the Auditor is bound to know everything the books tell him, to have all the suspicions the books suggest, and to make all the inferences to which all that he finds in the books would lead him. This, taken by itself, is a somewhat narrower view than has been previously suggested in the course of this chapter—namely, that the books must not be considered as the sole source of evidence—but it is thought there is very much less difference between these views than is at first apparent, and that the late LORD DAVEY's view that the Auditor should "have all the suspicions which a careful examination of the books would give him" amounts to very much the same thing as the opinion, already expressed in these pages, that the books themselves are *prima facie* evidence only, and must, in all cases of doubt, be verified by independent inquiry.

AUDITOR'S LIABILITY FOR DEFALCATIONS OF EMPLOYEES.—The question as to whether—and, if so, to what extent—an Auditor is liable to his clients for defalcations committed by their employees is one of very considerable importance, but unfortunately the precedents upon the subject are not sufficient to satisfactorily establish any general rule. The reports in *Ross v. Wright & Co.* (an Irish case decided in July 1896), and in *Wilde v. Cape & Dalglish*, and *Martin v. Isitt* (both of which will be found in Appendix "B."), may advantageously be consulted in this connection; but it cannot be

pretended that there is any degree of finality about them. Pending further decisions, however, it may perhaps not unreasonably be assumed that, in this (as in other) respects, the Auditor will be liable to be proceeded against by way of action for negligence in the discharge of his duties; and, if it could be shown that the defalcations had resulted from the negligence or incapacity of the Auditor, the probability is that he would be held liable in damages accordingly. The most interesting of the three cases in question is undoubtedly that of *Martin v. Isitt*, in which the plaintiffs claimed damages by reason of the fact that the monthly audit, which the defendants had contracted to perform, had been allowed to fall into arrear, and that the defalcations had remained undetected for a longer period than, in their view, was reasonable. The case was eventually settled without any definite expression of opinion upon the part of the Judge as to its merits; but doubtless, in so far as the delay in the monthly audit was unreasonable, the Auditor would be responsible for any loss incurred by his clients in consequence. The question is obviously, therefore, one of the very greatest importance, as showing the extreme desirability of monthly and other periodical audits being punctually proceeded with. On the other hand, a reasonable margin would, no doubt, in all cases be allowed. It would be manifestly impossible for an Auditor to commence his investigations in all cases *immediately* after the period had elapsed, and consequently it is only reasonable to suppose that some elasticity would be used in applying the general rule; otherwise the position of professional Auditors, say, in the month of January, would be a serious one.

With regard to the later decision upon the liability of Auditors, in the event of defalcations on the part of employees given by the Irish Court of Appeal in the case of the *Irish Woollen Co., Lim.* (a full report of which appears in Appendix "B"), it is important to bear in mind that the decisions of this Court are not legal precedents in England; but, be that as it may, it is thought that the proposition previously

advanced can now be entertained with even less doubt than before—namely, that where loss is incurred through the defalcations of employees, which defalcations might have been discovered or prevented by the exercise of due diligence, the Auditor will be liable. It may also be mentioned that in this case stress was laid in the agreement between the Auditor and the company that there should be a “monthly” audit, although there appears to have been some conflict as to what was actually intended by this arrangement. The circumstances were as follow:—

Dividends had been paid out of capital on the faith of accounts which were afterwards discovered to have been falsified, and the charge against the Auditor may (in effect) be divided under three headings:—

- (1) That he failed to discover that the stock had been over-valued.
- (2) That he failed to discover that the book debts had been over-valued.
- (3) That he failed to discover that the trade liabilities had been under-stated.

With regard to (1), the case would appear to be upon all-fours with the decision in the *Kingston Cotton Mills* case, and for much the same reasons the decision of the Court was in favour of the Auditor.

(2) Here, again, the Court decided in the Auditor's favour, on the ground apparently that he could not be held responsible for the insufficiency of the reserve provided against Bad Debts, nor for the omission to provide for Cash Discounts. With regard to Bad Debts, it is quite clear that all an Auditor can do is to make reasonable inquiries as to the sufficiency of the provision made, and the final responsibility must in all fairness rest with the directors and managers; but it would appear to be the duty of an Auditor to form a reasonable opinion as to the sufficiency of the reserve, and to qualify his report if in his

opinion such reserve is inadequate. Upon the subject of Cash Discounts it would not have been surprising if the Court had held that a proper provision *ought* to have been made for the amount which it was expected would eventually be deducted on payment of the various accounts, although, of course, *per contra* Cash Discounts might properly be deducted from the trade liabilities. In this respect the decision of the Court of Appeal is perhaps more favourable to the Auditor than might have been expected.

(3) It was in respect of his failure to discover that the trade liabilities were under-stated that the Auditor was held liable for negligence. There would seem to have been a systematic falsification of the books in this respect, and had this falsification been discovered at an earlier stage it would have been clear that the dividends paid away had not been earned. Incidentally, the discovery of falsification in the books under this heading would naturally have aroused suspicion as to the accuracy of the records under headings (1) and (2). Without having the actual books before one it is difficult—if not impossible—to express any opinion as to whether or not a reasonably careful and skilful Auditor could have discovered the frauds; but the report of the case distinctly suggests that there were points which would call for careful inquiry, and upon which in point of fact inquiry was actually made by the Auditor. He would appear to have noticed that certain invoices were not entered in the books until after the period to which *primâ facie* they related, and to have inquired as to why this course was pursued. The explanation given, apparently, was that the goods relating to these invoices had not been included in stock. The explanation is by no means unreasonable, as such a practice is certainly not contrary to the custom of many perfectly honest undertakings. In the *Kingston Cotton Mills* case it was stated that “Auditors must not be made liable for not tracking out ingenious and carefully-laid schemes of fraud when there is nothing to arouse their suspicion, and when these frauds are

perpetrated by tried servants of the company, and are undetected for years by the Directors." It may well be thought that these remarks would apply equally well to the *Irish Woollen Company* case; but it may be pointed out that the practice of "holding back" invoices because goods have not been taken into stock, although perhaps in itself permissible, is one which—considerations of fraud apart—might easily lead to mistakes. So that, if any means *are* available for checking the records of the transactions, such means ought not to be neglected by a reasonably careful Auditor. It appears that the suppression of invoices would have been at once discovered, had the Auditor taken the precaution of comparing the Creditors' Ledger Balances with the statements of account forwarded by the various creditors; and, that being so, it seems reasonable to have held that he was guilty of negligence in omitting to take this precaution. It is true that the "stock-taking" statements would only have disclosed "suppressed" invoices, and would not have thrown any light upon the invoices "carried over"; but the discovery of a large number of invoices altogether suppressed would at once arouse suspicion in the mind of any careful Auditor, and throw upon him the onus of further and more exhaustive inquiry. In the "soft goods" trade it is customary for creditors to be asked to send in "stock-taking" statements to be compared with the Creditors' Ledger Balances, so that particularly in the case of a concern carrying on such a business as that of the *Irish Woollen Company, Lim.*, does it seem reasonable that the Auditor should have been expected to take this precaution.

The most recent decision in connection with the liability of an Auditor for failure to detect defalcations is that in the case of the *London Oil Storage Company, Lim. v. Secar, Hasluck & Co.* (*vide* Appendix "B"), which came before the Lord Chief Justice and a special jury in June 1904. To the casual onlooker this case would appear to be quite straightforward, but Lord ALVERSTONE devoted so much care to his summing-

up that it seems clear the matter struck him as being one of more importance and more difficulty than to the ordinary observer appears to be the case. The principles governing the matter were, he said, clear, but the practical application of those principles to any individual case a matter of the very greatest difficulty. This admission is to be welcomed, as affording a most acceptable contrast to the manner in which the Courts regarded the views of Auditors a dozen years ago; but if the situation in the case referred to is so difficult as to seriously tax the intelligence of a special jury, it is clear that the present author was by no means overstating the case when—in the fourth edition of this work—he expressed the view that such important and such highly technical matters ought not, in fairness to Auditors, ever to be decided by a single Judge. Shortly stated, the points at issue here were as follows: During a number of years the defendants had never taken any steps to verify the amount of cash in hand appearing on the Balance Sheet. During those years the amount of this balance had very materially increased, and during the latter part of the period had not been shown separately from the balance at bank. Eventually, owing to the illness of the responsible cashier, it was discovered that the bulk of this balance was non-existent, with the result that the company sustained a loss of some hundreds of pounds. On behalf of the defence it was argued (1) that in the absence of suspicious circumstances an Auditor was entitled to rely upon the statements of trusted employees (*vide Kingston Cotton Mills case*); (2) that there were no suspicious circumstances here; (3) that the Directors had not had their suspicions aroused, and, therefore, if the case was one for suspicion, they were at least equally negligent; (4) that there was no evidence to show that the whole of the deficiency in the cash balance did not occur since the date of the last audit, in which case clearly the Auditor could not be responsible. The jury found that during the last four years the Auditor had committed a breach of his duty, and they assessed the damage sustained owing to this breach of duty at five guineas, adding as a rider

that they considered the Directors had been guilty of gross negligence. Upon the whole this verdict seems to be a very fair one, and certainly it cannot be said to err upon the side of severity. It is thought, however, that the defendants made their case worse by adopting too low a view of auditorial responsibility. There are, of course, many things that an Auditor *must* from time to time take upon trust; but under normal circumstances the balance of cash in hand seems to be the one asset in a balance Sheet that is really capable of absolute and unconditional verification. In the absence, therefore, of very exceptional circumstances—as, for example, in the case of an undertaking having numerous branches—the cash in hand should invariably be verified by the Auditor. The actual enumeration of the balance of cash in hand at each branch may not be practicable, but so far as can be gathered no such difficulty arose here; while again the very considerable increase of cash in hand (an increase in no way connected with the actual requirements of the business), ought, it is thought, to be in all cases regarded by the careful Auditor as a matter calling for careful inquiry, if not actually a matter for suspicion. That the Directors showed gross negligence in allowing such a large balance to accumulate in the hands of one of the employees of the company goes, of course, without saying; but it would be straining the decision of the Court of Appeal in the *Kingston Cotton Mills* case too far to suggest that, however negligent the Directors of a company may be, so long as *they* are satisfied the Auditor need inquire no further. Did that really represent the true limit of an Auditor's duties, those duties might be regarded as adequately discharged if the Auditor did nothing more than require the Directors to sign the draft Balance Sheet before he did so himself! It is obviously in the interests of professional Auditors that their duties should not be made unduly onerous, and that they should not be held responsible for the absolute accuracy of statements contained in the accounts which in the nature of things it is impossible for them to completely verify; but it is thought that it is equally in the interests of the

profession that, within such limits as may be practicable, the full responsibility of Auditors for the performance of their duties with reasonable care and reasonable skill should be rigidly enforced. On the subject of "partial" audits, see later (p. 357.)

LIABILITY OF AUDITORS FOR LIBEL.—The question of the liability of an Auditor for libel or slander is one which has not often been raised, but it would seem that the ordinary rules of law would apply hereto. That is to say, that, when the alleged libel or slander is true in point of fact, and is published by the Auditor in good faith and without malice, and in the *bonâ fide* discharge of his duty, it would, no doubt, be held to be privileged (*Lawless v. Anglo-Egyptian Cotton & Oil Co., Lim.*, 4 Q.B., 262). So far, the proposition is eminently satisfactory; but there still remains for consideration the position of the Auditor, assuming that he were mistaken in his facts, or assuming that he had—in all good faith—gone somewhat outside the actual scope of his duty in the particular matter. In these cases it is thought that the question would be primarily one for a jury to decide, but that every reasonable indulgence would be allowed to the Auditor who had acted in good faith and without malice. Against this, however, it may be mentioned that in the action of *Weiner v. Wurtemberg Electro Plate Company and another*, the plaintiff claimed damages against the defendants for libel, on the ground that the defendant company had instructed and authorised the co-defendants (a firm of Chartered Accountants) to issue a circular to their customers, stating, *inter alia*, that the plaintiff was no longer in their employ, and that "the bookkeeper had already been arrested on a charge of felony." Mr. Justice HAWKINS (now Lord BRAMPTON, P.C.) summed up in favour of the defendants, but the jury found a verdict for the plaintiff with £50 damages. The question as to whether or not an Auditor would be held liable in any particular case is thus really more dependent upon the vagaries of the jury concerned than upon any settled question of law, and the position is therefore, a highly unsatisfactory one.

It may be added in this connection that it is settled law that, when it is part of the duty of any persons to attend a meeting and to address it, any statements there made by them in good faith are privileged. Whatever an Auditor may state in his report to the shareholders, under Section 23 of the Companies Act 1900, is therefore clearly privileged. As to how far this would apply to verbal statements made by an Auditor at the general meeting of a company may, however, be reasonably doubted, inasmuch as it is by no means clear that an Auditor has any statutory right to attend general meetings. Indeed, it has been held by a County Court Judge that he has no such right; and, although this is a view from which probably some may differ, the point is by no means altogether free from doubt. It has certainly never been settled in the affirmative.

THE RESPONSIBILITY OF THE AUDITOR FOR ERRORS.—Having now discussed the practical extent of the Auditor's certification, it is time to pass on to a consideration of his liabilities, in the event of his investigation having failed to detect and expose errors or frauds.

CRIMINAL LIABILITY OF AUDITORS.—This is a question which need not long detain us, inasmuch as the reported cases are few and far between. In the *Portsea Island Building Society* case criminal proceedings were instituted against the Directors and the Secretary of the Society, but not against the Auditors. The Directors were, however, acquitted, and the case is only of interest in this connection, inasmuch as Mr. Justice HAWKINS (now Lord BRAMPTON) very clearly stated, in the course of his summing-up, that the evidence before him had established a *civil* liability upon the part of the Auditor.

In the case of the *Lancaster Building Society*, the Auditor, among others, was charged with various criminal offences, but was acquitted; and the Judge in his summing-up stated to the jury that, no matter how scandalous the negligence of an Auditor might be, they would not be justified in returning a

verdict of guilty unless they were satisfied that there was evidence of "not only criminal negligence, but also of fraudulent intent."*

The Auditors of the two Newfoundland Banks which failed in 1894 were also tried, in conjunction with the Directors of their respective companies, and likewise acquitted.

The case of *Regina v. Dexter and others* may be mentioned in this connection (*vide* Appendix "B"), but it throws no light upon the liability of Auditors, as the charges related to the promotion of a company that never even went to allotment. It has, however, an important bearing upon the liabilities of accountants who certify as to profits for the purposes of a prospectus.

At the trial of the Auditors and certain other officials of *Dumbell's Banking Co., Lim.*, which took place at Douglas, Isle of Man, in November 1900—the prosecution was under Section 221 of the Manx Criminal Code of 1872, but the wording of this section is identical with that of the English Act of 1862 (24 & 25 Vict., c. 96, section 84), so that the precise locality of the prosecution introduced no distinctive element—the defendants were convicted of having joined in the issue of false Balance Sheets, knowing them to be false, and with the intention to deceive, and were accordingly sentenced to varying terms of imprisonment.

If it were necessary to deal at length with the merits of this particular case, much space might be devoted to a discussion of the evidence, with a view to seeing whether the charges put forward were actually proved up to the hilt in all cases; but for the purposes of a general work of reference this is not required. It may be pointed out, however, that under Section 28 of the Companies Act 1900 any person who "wilfully makes a statement false in any material particular" in "any return, report, certificate, Balance Sheet, or other document, required by or for the purposes of" that Act, "knowing it to

* This of course was before the Companies Act 1900 was passed.

be false," is guilty of a misdemeanour, and liable on conviction to fine or imprisonment. This section goes somewhat further than the Act of 1862, inasmuch as it is no longer necessary to prove *intent* to deceive or defraud; but it is thought that the distinction is more apparent than real, seeing that anyone who wilfully makes a false statement, "knowing it to be false," would invariably be assumed by an average jury to have made it for some purpose, and it is unlikely in the extreme that the purpose would be an innocent one. Practically, therefore, the law probably stands exactly where it did before the passing of the 1900 Act, save that possibly the trial of any person charged thereunder might now be somewhat shortened.

Another criminal case which is of interest in this connection, although the Auditors were in no way involved, is the trial of the Managing Director and Breweries Manager of *Showell's Brewery, Lim.*, in March 1904, on various charges of fraud. The defendants, who were convicted and sentenced respectively to fifteen months' and nine months' imprisonment had for many years systematically overvalued the stock-in-trade and had induced subordinate employees of the company to certify to these valuations on the representation that they were more than covered by existing Secret Reserves. The case is, it is thought, chiefly of interest to Auditors in that it draws attention to a possible very serious abuse of Secret Reserves, and emphasises the importance of an Auditor very carefully inquiring into the circumstances under which recourse is had to such Reserves during "lean" years to conceal the comparatively poor results then achieved. It has been stated in some quarters that if the False Statements (Companies) Bill 1904, already referred to, were passed, it would be impossible for Directors to ever maintain a Secret Reserve without committing a criminal offence. This, it is thought, is an exaggeration. It is, however, important that both Directors and Auditors should bear in mind that the mere fact that Secret Reserves (*q.v.*) exist proves that, to some extent at least, the Directors are not entirely candid with their shareholders; and

the absence of absolute candour naturally necessitates at the very least the most scrupulous care in connection with all matters relating to the accounts.

CIVIL LIABILITY OF AUDITORS.—There are two kinds of procedure under which civil proceedings may be taken against Auditors for damages occasioned by negligent or unskilful discharge of the duties imposed upon them—namely, by way of action, and by way of misfeasance summons.

PROCEDURE BY WAY OF ACTION.—One of the leading cases under this procedure is the *Leeds Estate Building and Investment Society, Lim. v. Shephard*, which was decided by STIRLING, J., in 1887. This case will be found duly reported in Appendix “B,” and should receive the careful attention of the reader on account of its importance. The head-note of the official report is also of considerable interest; it reads as follows:—

“Held, that it was the duty of the Auditor in verifying the accounts of the company, not to confine himself to verifying the arithmetical accuracy of the Balance Sheet, but to inquire into its special accuracy, and to ascertain if it contained the particulars specified in the articles of association, and was properly drawn up to contain a true and accurate representation of the company's affairs.”

That portion of the judgment which more particularly affects Auditors enforces the same doctrine in even more definite terms:—

“In each of (these) years, L. (the Auditor) certified that the accounts were a true copy of those shown in the books of the company. That certificate would naturally be understood to mean that the books of the company showed (taking, for example, the certificate for the year 1879) that, on the 30th April 1879, the company was entitled to ‘moneys lent’ to the amount of £29,515 15s. od. This was not in accordance with the fact; the accounts, in this respect, did not truly represent

the state of the company's affairs, and it was a breach of duty upon L.'s part to certify as he did with reference to them. The payment of the dividends, directors' fees, and bonuses to the manager actually paid on those years appears to be the natural and immediate consequence of such breach of duty; and I hold L. liable for damages to the amount of the moneys so paid."

The futility of an Auditor attempting to escape his just responsibilities by a limitation of the scope of his certificate is here most forcibly demonstrated; there are, however, two other points, which must not pass unnoticed.

FIRST, there was no question, in this case, as to the accounts being false. The matter in dispute was no moot question of depreciation, or of apportionment between Capital and Revenue; the accounts were indisputably false, and it was not even suggested that the Auditor had done his best to verify their accuracy.

SECONDLY, the immediate result of his neglect was a payment of dividends, directors' fees, and bonus. Had no such result taken place, it is by no means so certain that any liability would have accrued.

Before dismissing this case altogether, it may be well to remark that the defendant was allowed the benefit of the Statute of Limitations; but—inasmuch as this point was not disputed by plaintiff's counsel, and was consequently not before the Court—it does not follow that a like plea would avail upon another occasion.

Astrachan Steamship Company Case.—This was an action brought in the Palatine Court at Liverpool to recover damages from the Auditors on account of loss sustained by the company through the dishonesty of its manager. A settlement was arrived at by the parties, so that no new point was decided as to the liability of Auditors, but it may be mentioned in passing that the Vice-Chancellor expressed some hesitation as to his jurisdiction to try the matter, and only proceeded upon being

satisfied that he did so with the consent of all parties. In this case a group of steamship companies were administered by the same manager, who was eventually adjudicated bankrupt with a large deficiency, and subsequently convicted for embezzlement. It appeared that he was able to satisfy the Auditors as to the existence of the balance of cash in hand in the case of each separate company by producing to them a sufficient sum of cash, although it would have been impossible for him to simultaneously produce a large enough balance to cover the amount that ought to have been in hand in respect of all the companies that he managed. Apart from this, however, it appeared that he had made entries in the books of the Astrachan Company showing that he had borrowed certain sums from that company at interest, and the suggestion was that a transaction of this kind was sufficiently unusual to make it the duty of the Auditors to call the attention of the shareholders to the fact, more especially as—there being no board of directors—the shareholders were entirely dependent upon the Auditor for the protection of their money.

Smith v. Sheard.—The report of this case (decided by Mr. Justice BRAY and a special jury on 11th May 1906) is reproduced in Appendix "B," although it is feared that it will prove more confusing than instructive, inasmuch as the verdict of the jury would appear to be hopelessly wrong. The point here was as to whether an Accountant who had (as he said, inadvertently) charged for "auditing" accounts could be held liable for failure to detect fraud on the part of an employee, when his services as Auditor had been requisitioned for another purpose, and the audit was evidently agreed for as a "partial" audit. The moral of the case appears to be that "partial" audits should be charged for as such, and that the precautions omitted in the process of compression should be clearly agreed to in writing, as between auditor and client. It is, however, always easy to be wise after the event.

PROCEDURE BY MISFEASANCE SUMMONS.—The passing of the Companies (Winding-up) Act 1890 has had

a very important bearing upon the liabilities of the Auditors of companies registered under the Companies Acts with what may be called "normal" articles of association, and, indeed, most of the cases that have yet been decided upon this subject have been the result of procedure under this statute. It is therefore desirable to consider, before proceeding to further discuss the liabilities of Auditors, the precise nature of the provisions of the 1890 Act, and the circumstances under which they apply. The provisions in question are comprised in Section 10, which is as follows:—

10.—(1) Where in the course of the winding-up of a company under the Companies Acts it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager, liquidator, or other officer of the company, has misapplied or retained or become liable or accountable for any moneys or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may, on the application of the Official Receiver, or the liquidator of the company, or of any creditor or contributory of the company, examine into the conduct of such promoter, director, manager, liquidator, or other officer of the company, and compel him to repay any moneys or restore any property so misapplied or retained, or for which he has become liable or accountable, together with interest after such rate as the Court thinks just, or to contribute sums of money to the assets of the company by way of compensation in respect of such misapplication, retainer, misfeasance, or breach of trust, as the Court thinks just.

(2) The provisions of this section shall apply in the winding-up of any company under the Companies Acts whether the same is being wound up by or subject to the supervision of the Court or is being wound up voluntarily, and whether the winding-up commenced before or after the passing of this Act, and notwithstanding that the offence is one for which the offender may be criminally responsible.

The essential distinction between procedure by way of summons under the foregoing "misfeasance" section and procedure by way of action is that the former is technically a proceeding in the liquidation, and consequently, as a matter of law, all evidence available in the liquidation is evidence which can be produced in support of the summons. That is to say, that the evidence given by the respondents, either at a

public examination under Section 8 of the 1890 Act, or under a private examination under Section 115 of the 1862 Act, is evidence in the misfeasance proceedings against those particular respondents, although not against any co-respondents there may be to the same summons.

This is a form of legal procedure which is new to English jurisprudence, and also, it is believed, to that of any other civilised country. An analogy (although in a far smaller degree) exists, however, in connection with the French Criminal Law, under which a person who has been once arrested on a criminal charge is cross-examined by an examining magistrate (who is virtually a police-inspector), with a view to forwarding the case for the prosecution, and the answers given by the prisoner to such cross-examination are put in as evidence at the trial. There is, however, an automatic safeguard to the French system that does not obtain with misfeasance procedure—namely, that the verdict has to be delivered by a French jury, who certainly under no circumstances would allow itself to be bound by what—in this country—we are accustomed to look upon as the law of evidence; and, that being so, it might well be argued that it is absolutely necessary, if crime is to be prevented at all, that exceptional facilities should be afforded to the prosecution. In this country, however, no such circumstances apply. English juries would, ordinarily speaking, be seriously prejudiced *against* any defendant who was charged with contributing either directly or indirectly to a failure by which shareholders' and creditors' money had been lost; and although no jury could be called upon to try a misfeasance summons except by consent of all parties concerned, it is to be remembered that some of the earlier recorded decisions appear to clearly indicate a similar prejudice upon the part of the Judges. Lest this statement should be thought too strong, it may be pointed out here that of the three earliest cases when charges of misfeasance came before the Court in connection with Auditors, the Judge in the Court of First Instance invariably decided against

the respondents, while in two cases his decision was absolutely reversed in the Court of Appeal, and in the remaining case it was reversed in respect of one of the two years in which it was given, and the reasons for its being upheld in the other year were materially modified. In the more recent case of *Dovey v. Corey* (in *re The National Bank of Wales, Lim.*) the Court of First Instance (WRIGHT, J.) was again against the respondent, and his decision was upset by the Court of Appeal, whose judgment was affirmed by the House of Lords.

As a matter of fact, it seems obvious that, in the nature of things, it is impossible for any one Judge (who is a lawyer, and therefore not an accountant) to express an opinion that is really entitled to the respect of the community upon the question as to whether or not, under a given set of circumstances, an Auditor has done all that could reasonably have been required of him; and in this connection it may be added that probably no satisfactory solution of this extremely difficult problem will be arrived at until some procedure is formulated by which accountants themselves may be called in with a view to acting as assessors, if not as actual judges, upon such questions. There is ample precedent for this innovation in the Commercial Courts and the Admiralty Courts at the present time, and it must be conceded that no commercial or marine case could possibly raise more abstruse or more technical matters than the question as to whether or not, under a given set of circumstances, an Auditor had done his duty. For the present purpose, however, it will suffice to mention that, after some considerable experience in the Companies Winding-up Court, Mr. (now Lord) Justice VAUGHAN WILLIAMS must evidently have come round to the view just expressed, or he would not, in the misfeasance proceedings brought against the Directors of the *London & Colonial Finance Corporation, Lim.*, have expressed the opinion that it was far preferable for a jury—rather than any single Judge—to express an opinion upon the points which he was called upon to decide. It may be added in this connection that, as all the parties were not

desirous of submitting their case to the arbitration of a jury, his Lordship was compelled to hear it unaided, and eventually decided in favour of the respondents.

It is impossible, in the space here available, to enter into detail upon all the arguments which have been raised against the present procedure under misfeasance summonses; but, in addition to the cross-examination of the defendants without any corresponding right of examination-in-chief, and the inherent inadequacy of the tribunal before which they are arraigned, the two following may be shortly mentioned:—

In the first place, before the misfeasance summons can be issued at all, the leave of the Court has to be obtained. This is granted on *ex parte* statements made by the applicant, which are not statements on oath, or even statements of fact, but an advocate's summary of the case for the prosecution. The presiding Judge is therefore called upon to express—and does express—a *prima facie* opinion on the merits of the case before the evidence has been heard; and, in the nature of things, it is not humanly possible to expect him to altogether disabuse his mind of the impression which these *ex parte* statements have created. Indeed, one may go further and say that he has already committed himself to an expression of opinion that the applicant has a good case for proceeding. To allow that same Judge to preside at the subsequent hearing of the misfeasance procedure is as inequitable as it would be to allow a magistrate to preside at a trial over prisoners whom he had previously committed. The second objection to the present procedure is that it does not compel the applicant to define his case before coming into Court. In view of the altogether exceptional facilities possessed by the applicant for obtaining information, this appears to be wholly uncalled for in the interests of even the strictest justice; moreover, it not only greatly increases the costs upon both sides (which under no circumstances are payable by the applicant personally), but, further, it makes the cost of these proceedings so enormous as to greatly encourage applicants in launching upon highly speculative proceedings,

in the hope that the respondent will pay something in settlement, rather than face the necessary and inevitable expense. In the *National Bank of Wales* case (already referred to) it has been stated that, prior to the hearing of the appeal, the respondent (who eventually succeeded) at one time offered £25,000 in settlement, and that the costs from first to last exceeded £10,000.

Having now shortly reviewed the nature of misfeasance procedure, it is time to pass on to a consideration—necessarily short and imperfect—of the effect of the various decisions which have hitherto been given. All these decisions will be found fully reported in Appendix “B,” and should be very carefully studied. The probability is that most careful examination of the text of the various judgments will fail to deduce any satisfactory summary of the precise duty of an Auditor under general circumstances; but, such as they are, they afford almost the only guide that is at present available as to the legal responsibilities of an Auditor, and—unpractical as they are in many details—the Auditor who desires to be upon the safe side would do well to see that his investigation conforms with the views there laid down as far as possible. The following summary of the leading cases will be found of value:—

London and General Bank Case.—Here it will be seen, by a careful perusal of the judgments reprinted in Appendix “B,” that, in their Lordships’ view, the defendant failed in his duty, not in neglecting any necessary portion of his investigation, but rather in failing to acquaint the shareholders with the results at which he had arrived. It appears that, in the first instance, the Auditor drew up a very unfavourable report, of which he sent a copy to each of the Directors; but that he was subsequently induced to modify this report, and to issue to the shareholders a certificate that contained no reference to its existence. This, it appears, he was persuaded to do on the understanding that some reference would be made to the matter by the chairman at the general meeting, and because he was

assured that the publication of his report would ruin the bank. At the meeting no real reference was, however, made to the Auditors' report, and the Auditor (who was present) allowed the omission to pass and the dividend to be voted without any protest upon his part.

The Court of Appeal held that the Auditor had failed in his duty because—knowing what his report to the Directors proved that he knew—he failed to place the true position before the shareholders. It was held that his certificate (to the effect that the assets were “subject to realisation”) was no true warning of the actual position of affairs, and that the Auditor had no right to depute to the chairman of the Directors the giving of this warning to the shareholders. In paying the dividend in question the Directors had committed a breach of trust, “facilitated, and, indeed, only rendered possible by the Auditor, who failed in discharging his own duty to the shareholders.” It was therefore held (following the decision in the *Leeds* case) that the Auditor was jointly and severally liable with the Directors to repay the amount wrongfully distributed as dividend. It may be noted in passing that Mr. (now Lord) Justice VAUGHAN WILLIAMS' decision with regard to the dividend paid in 1891 was reversed; because, although the Lords Justices were satisfied that the accounts were incorrect, they were not satisfied that the Auditor knew—or by the exercise of due diligence ought to have known—that they were incorrect, and that no profit had been earned.

It is beyond the scope of the present work to deal with this decision further than as a precedent, and accordingly it is not proposed to consider this much-discussed case very fully. Still less is it proposed to embark upon either an attack, or a defence, of the Auditor's conduct. It would seem, however, that he was hit in this case for an offence which does not really appear to have amounted to more than an error of judgment, and that without any expert evidence being heard as to what is the usual course for Auditors to pursue under like circumstances. How far such expert evidence would have helped Mr. THEOBALD is,

however, a point upon which some doubt may reasonably be felt. The view adopted by the Court of Appeal—namely, that the Auditor's duty is to report to the shareholders—is logically unassailable, and it may perhaps be noted in passing that it is the view that has been strongly expressed throughout this work from the publication of the first edition to the present time.

The Kingston Cotton Mills Case.—This was a summons taken out by the Official Receiver, as liquidator of the company, applying for a declaration that the Directors and Auditors of the company had committed misfeasance in sanctioning the payment of dividends, on the grounds (1) that the value of the mills owned by the company, as stated in the published accounts, was greatly in excess of their actual realisable value; (2) that the value placed upon the stock-in-trade in the published accounts was greatly in excess of the actual realisable value of such stock as existed at the time. The case in the first instance came before Mr. (now Lord) Justice VAUGHAN WILLIAMS, who decided he was bound by the previous decisions in the *Neuchâtel Asphalte* case, the *Commercial and General Trust* case, and in *Wilmer v. McNamara & Co., Lim.*, and could not, therefore, hold that it was necessary for a company to write down the value of its fixed assets to a figure which they might reasonably be expected to realise. With regard to the stock-in-trade, however, he held that, in point of fact, the stock sheets had been falsified by the Managing Director, whose certificates as to the quantities and value of such stocks had been accepted by both the Directors and the Auditors—the latter drawing attention to this fact in their certificate. He held that it was reasonable for the Directors to accept the statements of the Managing Director, but that, in the circumstances of the case, it was not reasonable for the Auditors to do so. He therefore held the Auditors liable, but not the Directors. In giving his decision, his Lordship was doubtless greatly influenced by the evidence given by an examiner attached to the Official Receiver's department of the Board of Trade, which was to the effect that a careful examination of the accounts would have shown that the percentage of gross profit

disclosed by the Trading Accounts was so absolutely abnormal as to reasonably call for further inquiry; and a great deal might doubtless be said in favour of this view, assuming the accuracy of the facts already stated. It is, no doubt, the duty of an Auditor to thoroughly scrutinise accounts before certifying them, and if they show upon the face of them what is apparently an extraordinary state of affairs, it seems not unreasonable to suppose that the duty is cast upon the Auditor of inquiring further into the matter; for, although it may not be the duty of an Auditor to be suspicious, it will probably be generally accepted as a statement of principle (following the words of the late Lord DAVEY) that "the Auditor is bound to know everything that the books tell him, to have all the suspicions that the books suggest, and to make all the inferences to which what he finds in the books would lead him." In this case it might be held that a careful scrutiny of the accounts would have suggested suspicions, which, if once aroused, should have been thoroughly inquired into; but, against that, it must be borne in mind that Mr. Justice VAUGHAN WILLIAMS had before him the evidence of an examiner who had had upwards of two years in which to make his investigation of the accounts, and that (combined with the fact that the investigation was made after the failure of the company) may well account for facts having then come to light which it could hardly be reasonably expected an Auditor would, in the ordinary course of business, have ascertained. Be this as it may, however, the decision was afterwards reversed on appeal. The case for the appellants was argued before the Court of Appeal (consisting of Lords Justices LINDLEY, LOPES, and KAY) on the grounds (1) that the Auditors had not failed to discharge their duty to the company, and were under no liability to make good the money misapplied; (2) that, even if they had, the proper remedy was by way of action, and not by the summary process to which the liquidator had recourse. The Court decided to dispose of the second objection first. With regard to this, Lord Justice LINDLEY said that it had already been decided that the Auditors of this particular company were officers within the meaning of Section 10 of the 1890 Act. The object of that section was to

facilitate the recovery by the liquidator of assets of a company improperly dealt with by its promoters, Directors, or other officers. The section applied to breaches of trust and misfeasances by such persons. His Lordship agreed that the section did not apply to all cases in which actions by the company might lie for the recovery of damages against the persons named; it was easy, he said, to imagine cases of breach of contract, trespasses, negligences, or other wrongs to which the section was inapplicable, and some such had been the subject of judicial decision. But he was not aware of any authority to the effect that the section did not apply to the case of an officer who had committed a breach of his duty to the company, the direct consequence of which was a misapplication of its assets, for which he could be made responsible by an action at law or in equity. Such a breach of duty, if established, was a "misfeasance" within the meaning of Section 10, and, therefore, the procedure adopted by the Official Receiver in this case was not improper. This part of the Court of Appeal's decision is of some importance, as tending to show that, where it can be established that the Auditor of a company is an "officer of the company" within the meaning of Section 10, then any charge of negligence which can be brought against him in respect of the audit may, apparently, always be dealt with by way of misfeasance summons.

Passing on, however, to the merits of the case, Lord Justice LINDLEY took quite a different view to that adopted by the Court below. He pointed out that "an Auditor was not an insurer," and that in the discharge of his duty "he was only bound to exercise a reasonable amount of care and skill." What was a reasonable amount of care and skill in any particular case "depended upon the circumstances of that case; and, if there was nothing which ought to excite suspicion, less care might properly be considered reasonable than would be so considered if suspicion was, or ought to have been, aroused." In particular, his Lordship "protested against the notion that an Auditor was bound to be suspicious, as distinguished from being reasonably careful."

Lord Justice LOPES said it was the duty of an Auditor to bring to bear on the work he had to perform that skill and caution which a reasonably competent, careful, and cautious Auditor would use. What was "reasonable care, skill, and caution" in any particular case "must depend upon the particular circumstances of that case." An Auditor, his Lordship said, "was not bound to be a detective; nor, as was said, to approach his work with suspicion, or with a foregone conclusion that there was something wrong. He was a watch-dog, but not a bloodhound, and was justified in believing tried servants of the company in whom confidence was placed by the company." If there was anything calculated to excite suspicion, it would be his duty to probe it to the bottom, but in the absence of anything of that kind, he was only bound to be reasonably cautious and careful.

The full text of their Lordships' decisions will be found in Appendix "B" to this volume. But it will be seen that, so far as any general principle is deducible therefrom, they are quite in accord with the views which have already been expressed in the present work.

The Western Steam Bakeries Case.—In this case the Official Receiver (as liquidator of the Western Counties Steam Bakeries, Lim.) took out a summons against Messrs. PARSONS & ROBENT. The preliminary objection was raised by the respondents that they were not "officers of the company" within the meaning of Section 10, inasmuch as they had never been formally appointed Auditors in accordance with the requirements of the company's articles of association; and although Mr. (now Lord) Justice VAUGHAN WILLIAMS declined to adopt this view it was the one eventually taken by the Court of Appeal, so the case was not further proceeded with. The fact that the Official Receiver did not think it worth while to proceed against the Auditors by way of action, after failing to secure a hearing to a misfeasance summons, shows clearly how much more unfavourable to the Auditor is the latter procedure than the former.

The National Bank of Wales Case.—This was a misfeasance summons brought against a Director for having permitted the payment of certain dividends without due provision for bad and doubtful debts. Mr. Justice WRIGHT held the Director liable, the Court of Appeal reversed the decision, and the House of Lords confirmed the latter view. The reasons advanced by the Court of Appeal in support of its judgment attracted much comment at the time, and were stated in the fourth edition of this work to be “somewhat extraordinary”; as, however, the case did not directly affect Auditors, it was not then thought worth while to discuss the matter at great length. The decision of the House of Lords (*vide* Appendix “B”) is, however, of more far-reaching importance. It upholds the judgment delivered by the Court of Appeal on 2nd August 1899, but expressly dissents from some of the conclusions then arrived at. The Supreme Court has held that it is no part of the duties of a Director to go into details, and that he is not responsible for the knavery or dishonesty of trusted officials of the company of which he had no knowledge at the time. The Law Lords, however, thought it desirable to express their dissent from those portions of the judgment of the Court of Appeal which declared the respondent Director not liable, because they (the Court of Appeal) considered that the dividends that had been challenged had not in effect been improperly declared; and, while approving the decision of the Court of Appeal in the case of *Verner v. The General and Commercial Trust, Lim.*, the House of Lords laid it down that the question as to what profits could be properly distributed by way of dividend in any individual case could only be certainly determined when that case arose for decision. It was added that, although the provisions of the Companies Act 1877 (with regard to the reduction of a company’s capital) must not be ignored, it did not necessarily follow that a company was obliged to make good the losses incurred in previous years out of subsequent profits before distributing anything by way of dividend.

This decision is of the greatest importance, as it removes the disturbing element occasioned by the judgment of the Court of

Appeal, and for practical purposes replaces the whole question as to what are divisible profits upon a sound commercial basis. In the course of the judgment it was, indeed, intimated that, in deciding any particular case involving this question, the Courts would have to take into consideration the views of men of business specially versed in such transactions as those engaged in by the particular company under review.

Re Joseph Hargreaves, Lim.—In this case misfeasance proceedings were taken against the Auditor for having improperly sanctioned the payment of dividends out of capital. The circumstances are somewhat unusual, in that, although it is not disputed that dividends were improperly declared, it appeared that the Auditor had never certified the accounts, and had systematically protested to the Directors against the declaration of any dividend. No general meeting of the company had been convened, so that it was impossible for the Auditor to place his views directly before the shareholders. Mr. Justice COZENS-HARDY (now M.R.) held that the Auditor had performed the whole of the duties of his position. The case is therefore of especial interest, as showing that it is no part of an Auditor's duty to communicate with shareholders otherwise than through the medium of the general meeting; and, further, that, even where there are such serious irregularities as the failure to convene a general meeting for several years in succession, it is not incumbent upon an Auditor to resign his position and to refuse to have anything further to do with the concern. This decision would appear to still hold good, notwithstanding the subsequent passing of the Companies Act 1900.

POSSIBLE LIMITS TO LIABILITY.—It has already been stated that, in the cases quoted above, the measure of damages incurred by the negligent Auditor has been the full amount wrongfully paid away in dividends. This raises the very important questions as to how far these cases can be relied upon as precedents in the event of the Auditor's negligence being proved, but

- (1) *No* dividend having been paid ;
- (2) A dividend having been paid, and the company having since gone into liquidation, but there being sufficient assets to pay all costs and all creditors in full.

It is hardly to be supposed that in either of these cases the Auditor would incur *no* liability, but a very little consideration will suffice to show that a different mode of assessing damages would have to be adopted. It may be added here, however, that although the practice of the Courts has hitherto been to give judgment jointly and severally against all respondents held liable for the full amount of dividends improperly paid, with costs (without any corresponding right of contribution *inter se*), it by no means follows that this course will always be pursued. The language of Section 10 is "to repay any moneys . . . misapplied . . . or to contribute such sums of money . . . as the Court thinks just."

In this connection the decision in *re Moxham v. Grant* (*vide* Appendix "B") will be found of interest. Here the Directors had been found liable to refund to the liquidator of the company certain dividends improperly paid out of capital, under circumstances which conveyed to the shareholders a knowledge of the nature of the source from which dividends were declared. It was held that the Directors had a right to recover from the various shareholders the amount of their respective dividends.

It may be added that in one case, where judgment was given in favour of the Official Receiver on a misfeasance summons, he was directed only to enforce that judgment so far as might be necessary to secure the repayment of twenty shillings in the £ to contributories. The decisions in *Boaler v. Watchmakers' Alliance, &c., Lim.*, and *Towers v. African Tug Company, Lim.* (*vide* Appendix "B"), also impose limits on the shareholders' right of recovery against Directors.

To sum up, it does not appear that (assuming the Official Receiver, or other liquidator, is acting *bonâ fide*, and not

actuated by malice) the conscientious and capable Auditor, who has endeavoured to conduct his audit upon the lines laid down in this work, need feel much apprehension as to the legal consequences arising either from a *bonâ fide* error of judgment, or from his inability to discover an exceptionally clever fraud. On the other hand, it is, doubtless, greatly to the advantage of all properly qualified Auditors if a reasonable measure of responsibility be expected from them, for there is then some chance of scaring out of the field a too-numerous class of so-called Auditors, whose extreme ignorance of the veriest elements of their profession is only equalled by their utter inability to appreciate the moral responsibility of their position. It is, no doubt, open to question whether the initiation of proceedings should not be vested in some higher and more responsible authority than at present, and there is serious room for complaint against the harshness and inequity of misfeasance procedure generally; but it is believed that abuses rarely occur, and that, consequently, all competent and reputable Accountants may regard the matter as something that does not in any sense intimately concern them.

DUAL APPOINTMENTS.—When two Auditors have been appointed, each is jointly and severally responsible for the proper conduct of the audit, unless the contrary is clear from the terms of the appointment. When the appointment by statute provides for two Auditors, the appointment of a firm of two or more partners is not a due compliance with the statutory terms; but the appointment of two individual members of the same firm will serve. In the case of an undertaking having operations abroad, the employment of a local Auditor to verify the local accounts imposes no liability upon the Auditor of the company, provided the latter is careful to indicate in his report exactly how far his personal verification has extended, and provided he has exercised due diligence and honestly believes the truth of the information he has accepted at the hands of the local Auditor.

CHAPTER XI.

INVESTIGATIONS.

IT has been thought desirable to devote a chapter to that special class of audit that is usually known as an "Investigation." The subject is one intimately connected with auditing, but possesses many peculiar features which cannot afford to be overlooked.

OBJECTS OF INVESTIGATIONS.—An investigation—so far as present purposes are concerned—may be described as "A special audit, undertaken for a particular purpose." The particular purposes for which an investigation is usually made are as follow:—

I. Upon the sale of an undertaking :

- (a) To a public company.
- (b) To a private purchaser, or purchasers.
- (c) To a continuing partner, or partners, by a retiring partner, or partners.

II. For the purpose of obtaining special information as to the position of an undertaking :

- (d) On behalf of a committee of investigation appointed by shareholders.
- (e) On behalf of a present or prospective creditor.
- (f) With a view to the discovery of suspected fraud.

The former group alone claims attention in this work.

EXTENT OF INVESTIGATIONS.—When making an investigation of any kind it must not be forgotten that those relying upon the Accountant's report will naturally, and indeed reasonably, take it for granted that, so long as they adequately explain their object in seeking his assistance, it is for him, as an expert, to decide both as to the nature and the extent of the examination itself ; and, in the event of it being subsequently discovered that an investigation had failed to achieve its intended object, it would be for the Accountant to show that such failure did not arise from any cause which could have been prevented by a more complete, or a more exhaustive examination. Cases are not unknown in which a faulty investigation has been attempted to be shielded under the plea that special instructions had been given by the client, and that such instructions had been duly carried out ; it being argued that where the client has given special instructions as to the course to be pursued, the Accountant must be exonerated from any mishap arising from the defectiveness of those instructions. This doctrine appears to be a most dangerous one. There can be no doubt that whatever instructions the Accountant may have received were intended rather as a description of the object to be effected than as a definite requirement as to the means by which that object was to be attained. It goes without saying that the best authority as to the means to be employed must be the Accountant himself (who receives his instructions by virtue of his being an expert in the matters requiring investigation), and it would thus seem that—however desirable it may be that he should receive, and even welcome, suggestions as to the *modus operandi* of his work—an Accountant cannot submit his professional discretion to the dictation of his clients without sacrifice of self-respect and grave danger to his clients' interests. An Accountant who undertakes the responsibility of an investigation ought not to seek to shield himself from the implied responsibility of proceeding upon that investigation on the lines which his professional experience convinces him are the proper ones.

The position of the investigating Accountant, when only incomplete sets of books are available, is a question of very considerable importance. So long as the books are sufficiently complete to enable the Accountant to reasonably arrive at the conclusion that (so far as they go) they are accurate, there can, it is thought, be no objection to his issuing a report confined to such matters as the books may show. But there is a danger of the whole system of investigation falling into discredit, if Accountants go too far, and substitute for certificates of actually accomplished facts statements so qualified as to amount, in effect, to but little more than a carefully safeguarded expression of opinion. It should be borne in mind that the object of any form of Accountant's certificate or report, included in a company prospectus, is to satisfy intending investors, and that such persons do not, as a matter of fact, by any means always carefully study the wording of the report, or certificate, referred to. Unless, therefore, an Accountant has really something to certify he should studiously refrain from issuing any statement of opinion, or estimate, in the form of a certificate.

DETECTION OF ERRORS IN THE BOOKS.—Before proceeding to consider the subject in further detail, it would appear desirable to clear up a point which is of the greatest importance, and upon which a considerable difference of opinion appears to exist—viz., the position of the Accountant who has certified as to profits which, in consequence of the falsification of the accounts investigated, have subsequently proved to have been over-stated. There appears to be no decision directly bearing upon this point; but a case which came before Lord KYLLACHY at the Court of Session in Edinburgh, in 1892, is of considerable interest. The case was that of the *Edinburgh United Breweries, Lim., &c. v. James A. Molleson (Nicholson's Trustee), &c.*, and the question then at issue was as to whether the circumstance that the profits disclosed by the books of the Palace Brewery, Edinburgh, were in excess of the amount actually made was (in the absence of

fraud on the part of the vendors) a sufficient ground for the cancellation of the purchase, or for damages. It will be seen that this case has only an indirect bearing upon the point now being considered; indeed, the interest which it possesses is dependent rather upon the nature of the evidence than upon the point actually at issue. Especially must it be borne in mind that, although Lord KYLLACHY'S decision was upheld upon appeal, it was merely upheld because it was considered that the plaintiff had no right of action against the defendant, no opinion being expressed by the Court of Appeal upon Lord KYLLACHY'S views. At the original hearing of the case it was contended on the one side that books submitted to Accountants for examination were to be taken as warranted free from falsification; while, on the other hand, it was argued that it was not the custom for any such warranty to be implied, and that a proper investigation of the accounts should have disclosed the fact that the profits had been, more or less, over-stated. In giving his judgment, his Lordship stated that it appeared to him that the question was as to whether it was a condition of the contract of sale, expressed or implied, that the books of the brewery were to contain no errors, or, at least, no errors that were not easily to be discovered, and he confessed his inability to discover any reason for so holding. He could find no standard according to which the purchaser's examination of the books was to be conducted, and he was, therefore, unable to hold that the plaintiffs were entitled to reopen the contract, and now raise the question as to whether a condition as to the amount of profits had been fulfilled. The chief point in this decision which is really of interest in the present inquiry is the finding that there does not exist in a contract for sale based upon a statement of profits an implied condition that such statement is correct. Exception must, of course, be taken in the case of a fraudulent misstatement, for naturally such contracts would be voidable upon proof of fraud. The question remains, however, that if the vendors have acted *bonâ fide* there is no redress for the purchasers if they have given too large a price for an undertaking in consequence of an incorrect

statement of profits by the vendors (provided the purchasers have had an opportunity of verifying such statement), or in consequence of a statement of profits that has been falsified—it may be by some employee of the vendors, unknown to them. It would therefore appear that, in such a case, an investigation that failed to reveal the actual condition of affairs would have failed to achieve its most important object. In the case of *Short & Compton v. Brackett* (*vide* Appendix “B”) it was expressly decided by Judge TINDAL ATKINSON that an investigating Accountant is entitled to “assume” the accuracy of the figures appearing in the books.

Opinions of Accountants thereon.—It is not proposed to fully discuss the legal position and responsibilities of an investigating Accountant under such circumstances, nor to criticise the investigation that was made in *The Edinburgh United Breweries’* case; but as there is much that is deserving of attention in the various opinions that were expressed by the expert witnesses who appeared in that case, the opinions of these witnesses are shortly stated here.

Mr. WM. H. KING, F.C.A., considered that there is a difference between checking books and investigating profits, and that an investigation of profits, even if properly conducted, would not always reveal an actual misstatement thereof.

Mr. T. P. LAIRD, C.A., gave it as his opinion that in making such investigations he did not consider it any part of his duty to go through all the books and vouchers as in the case of a regular audit.

Mr. JAMES ALEX. ROBERTSON, C.A., stated that, in investigating the profits of a business with reference to a sale, his experience was that an Accountant was not expected to check the books and entries for the purpose of tracking falsifications. There was a marked difference between an audit and an investigation with a view to profits. The falsifications in this case could not have been discovered without a comparison of the postings in one set of books into another, and he held that it

was no part of the duty of an accountant turned on to investigate profits. Personally, he always inserted the words "assuming the accuracy of the books" in his certificates.

Mr. FREDERICK WILLIAM CARTER, C.A., expressed himself as being of the same opinion as Mr. ROBERTSON.

Mr. WM. GRAHAM (of the firm of NICHOLSON, GRAHAM & GRAHAM, solicitors) expressed his opinion that Accountants, when instructed to investigate into the profits of a company, were not expected to go into such details as would have been necessary to discover the falsifications in this particular case.

Mr. ALEXANDER YOUNG, F.C.A. (Messrs. TURQUAND, YOUNGS, BISHOP & CLARKE), said that it was not the custom in such cases to examine the books in detail. Accountants considered that they were entitled to assume the genuineness of the books.

On the other hand,

Mr. JAMES A. MOLLESON, C.A., thought that a proper examination would have discovered the falsifications; he considered that an Accountant pursuing an investigation that would be useful would wish to *analyse* the accounts, and if this had been done the frauds would have been discovered.

Mr. RICHARD BROWN, C.A., also considered that the falsifications should have been discovered; he considered that an examination of the individual (trade) accounts was necessary to form a correct idea of the nature of a business, and had this been done the frauds would have been discovered.

Mr. DAVID SIMPSON CARSON, C.A., expressed himself as being of the same opinion as Mr. BROWN.

In speaking of the object of these examinations, the writer of an article that appeared in *The Accountant* at the time says: "What the public seem to want is, not the nearest approach to facts that can be obtained in so many days or weeks, but the nearest approach to facts that is humanly possible." This

will be found to accurately express the views of the average layman.

INVESTIGATION ON BEHALF OF PROJECTED COMPANY.—For the purpose of pursuing this inquiry in further detail it is proposed to narrow the field down to the question of investigations made on behalf of a projected company; and the most convenient method of dealing with the subject will be to contrast the methods to be adopted in such an investigation with those ordinarily employed in a regular audit.

From a theoretical point of view there need, of course, be no difference of method; for both audits and investigations aim at a complete disclosure of the facts. In practice, however, it is usual to restrict the inquiry, so far as is possible, without imperilling the efficiency of the examination; and it is because the objects of an audit are not altogether the same as those of an investigation that the method adopted in each case—*i.e.*, the abbreviated, practical method—varies somewhat.

LIMITS OF AN INVESTIGATION.—A regular audit professes to discover the true position of affairs. An investigation as to profits, made on behalf of a proposed company, professes to discover the position of affairs so far as they affect the particular object in view. In some respects the narrower field of an investigation will permit the Accountant to reduce the scope of his examination; but, on the other hand, there would appear to be many points upon which a greater strictness of inquiry is necessary. Thus, supposing the Accountant to be acting upon behalf of the purchasers of an undertaking, he may take it for granted that the accounts submitted to him by the vendors do not under-estimate the profitable nature of the business, or the strength of its financial position. Consequently, it does not seem necessary that he should inquire with the same exhaustiveness that he would use in the case of an audit into the completeness with which every source of income has been duly accounted for; neither does it appear necessary

for him to consider the validity of the various items of expenditure charged in the accounts, nor to check such expenditure minutely with the vouchers. On the other hand, if he is acting on behalf of the vendors, it is clearly desirable that both these points should receive careful attention, but in that case the investigation would not differ greatly from the complete audit; for it is obvious that he could not authorise the submission of accounts to the proposed purchasers until he was satisfied that such accounts were true in all respects.

FRAUD IN ACCOUNTS.—Yet another difference between investigations and audits will not fail to strike the observer. An ordinary audit must always aim at the discovery of fraud; but an investigation as to profits would not appear to involve any such inquiry, except in so far as the assets or profits might have been fraudulently over-stated for the purpose of concealing defalcations, or of deliberately making the accounts appear unduly favourable.

Broadly speaking, there are two ways in which books may be falsified for the purpose of concealing fraud. The first method is by falsifying the Balance Sheet, either over-stating assets or under-stating liabilities to cover the amount stolen; the second method is by falsifying the Revenue Account, by under-stating income or over-stating expenses, so that the profit shown by the books may be reduced to the profit which was actually netted by the proprietors, after deducting the amount misappropriated by the defaulting official.

If the first method has been adopted, the purchasers will not necessarily be prejudiced, for the profits shown by the books will have been the profits actually made; while the assets which appear in the books at an unduly inflated price will usually be guaranteed as to value by the vendors, or else vouched for by the certificate of an independent valuer. Sometimes, however, the investigating Accountant assumes responsibility for the accuracy of the scheduled book debts taken over by the proposed company, and in such cases it

will, of course, be necessary for him to carefully inquire into their correctness.

On the other hand the defalcations, if considerable, are likely to be concealed by a falsification of Balance Sheet items rather than of Revenue items, for any material under-statement of profits, such as would be involved by the last-named form of falsification, would be extremely dangerous, as drawing prominent attention to the existence of a leakage. A falsification of Balance Sheet items, with a view to concealing defalcations, ought not to escape the attention of the investigating Accountant: not, of course, because he is necessarily responsible for the values attached to the various assets and liabilities in the Balance Sheets of the undertaking about to be purchased, but because he cannot safely include, in his certificate of past profits, profits actually earned by the undertaking which, owing to the dishonesty of its employees, never went into the pockets of its proprietors.

Under the second method it would appear that the purchasers would actually gain by the defalcations of an official of the vendors, for the profits earned would be in excess of those shown by the books, while the latter would form the basis upon which the purchase price for Goodwill was calculated; and, as the Balance Sheet would correctly record the financial position, there would obviously be no injustice done to the purchasers if these figures were taken as a basis for valuation. It is thought, therefore, that the investigating Accountant acting on behalf of a proposed company need not trouble to go exhaustively into the question of the *bona fides* of the various expenses debited, his great object being to make sure that the expenses are completely recorded in the books submitted to him. On the other hand, he will require to look carefully into the *bona fides* of many transactions, which the Auditor would naturally pass either unquestioned, or, at all events, after due representation of the circumstances to his clients. The difficulty of the investigating Accountant's position arises from the fact that his real clients (*i.e.*, those in whose interests he is acting)

are an unknown, and, at that time, non-existent body. It is, therefore, obviously impossible for him to consult them in any way during the course of his investigation, and his only means of acquainting them with the result of his inquiry will be by means of his certificate.

SCOPE OF CERTIFICATE.—In making an investigation as to profits, therefore, the Accountant must be careful never to lose sight of the object for which his investigation is being made. That object may be said to be to ascertain

- (a) Whether the business of the vendors is worth purchasing.
- (b) Whether such business is worth the price asked for it by the vendors.

The Accountant is not actually asked to express a definite opinion upon either of these points, for it is obviously the business of each intending shareholder to answer these questions to his own satisfaction before applying for shares, but it is pointed out that the Accountant's certificate forms almost the sole basis upon which the shareholder can judge of the prospects of the proposed company, and it is therefore argued that it should be the Accountant's aim to so conduct his investigation, and so frame his certificate, that the materials necessary for a correct judgment may be placed before the public. At the same time it cannot be too strongly insisted upon that an Accountant's certificate as to profits, relating as it does to past events, deals with a subject-matter that ought to be capable of absolute verification. The certificate, therefore, should be a clear and unconditional certificate of accomplished facts, and not a mere estimate of possible—or even probable—future results, misnamed a "certificate." To the limited extent already mentioned it may be permissible, and even desirable, to modify the past results so that they may more usefully serve the purpose for which they are primarily intended—namely, provide a reliable index of future profits. But at the same time a certificate should relate not to the future, but to the

past; and intending investors would do well to bear in mind that, unless a definite statement as to the past *is* provided in a company prospectus, the reasonable assumption is that the past profits have been unsatisfactory.

There is yet another point which the Accountant must not fail to bear in mind. Inasmuch as he may be required at any future date to substantiate the statements that he has certified, he should not fail to make the most copious notes of all that transpires during the course of his investigation. These notes should not be confined to actual figures and calculations: whatever explanations he may have received in reply to his inquiries should be committed to writing, so that they may be available if required. If this be not attended to, and legal proceedings are subsequently instituted requiring the Accountant to substantiate his report, his position will not be an enviable one, for he will probably have to go over at least a portion of the ground a second time, and perhaps some of the evidence he formerly utilised may no longer be available.

LENGTH OF PERIOD TO BE INVESTIGATED.—

It is generally held that it is no part of the Accountant's duty to prescribe the term of years over which his inquiry should extend. It is, however, desirable to bear in mind the importance of expressly stating in the certificate the period that has been covered by the investigation; and, further, it is absolutely essential that the inquiry should be brought reasonably up to date. It may be found convenient to report only upon the results of completed years, but the odd months elapsing between the date of the last Balance Sheet and the date of the investigation should not escape notice, and if they show any material falling-off, the fact ought not to escape attention. It may be added here that it is very desirable that the Accountant's certificate should separately state the profits of each year covered by the investigation.

METHOD OF PROCEDURE.—STANDING OF VENDORS.

—Before actually commencing an investigation it is very

desirable to make inquiries as to the position and character both of the promoters and the proprietors of the undertaking. A man is always apt to be known by the company he keeps, and no one can afford to be mixed up with persons of more or less doubtful reputation. Moreover, if a man bears a really bad character, it may safely be taken as being at least probable that the company in which he is concerned is not likely to prove a very good investment to the public ; and an Accountant is not likely to do himself much good by mixing himself up with unprofitable companies.

SYSTEM OF ACCOUNTS.—The next point that claims attention is the general system upon which the books have been kept. And, in this connection, it may be mentioned that—inasmuch as it is very desirable that the Accountant should secure the co-operation of the employees of the establishment—it is a mistake for him to abuse the system of accounts which he finds in use, in the presence of the bookkeeper. Any such want of tact upon his part is almost certain to put the bookkeeper's back up, and then, instead of information flowing in smoothly, it has to be dragged out by a course of cross-examination that involves a heavy expenditure of both time and temper.

AUDITED ACCOUNTS.—If the books have been regularly audited by a Chartered Accountant it is a good plan to seek an interview with him, and endeavour to gather the precise extent of his examination, and also his general opinion upon the matter. This course is, perhaps, somewhat unusual ; but clearly it cannot be regarded as objectionable, while cases may easily arise in which it might be a most useful course to adopt. For instance, if a thorough audit has been made at regular intervals by a competent and trustworthy Accountant, the investigating Accountant might feel fairly safe upon most matters of mere arithmetical accuracy, and confine his attention more exclusively to questions of principle and to values.

UNAUDITED ACCOUNTS.—On the other hand, if there has been no regular audit, and *a fortiori* if the books have not

even been regularly balanced, it seems as though he could not, with safety, neglect an absolutely exhaustive inquiry into all the facts. Of course, objections may be raised to this position, the most important being the objection that such a complete examination would occupy a much longer time than is ordinarily available for the purpose. It is, however, submitted that it is the Accountant's duty to make an effective investigation—not the most effective investigation practicable in a limited period of time—and, further, that he should so conduct affairs that he need not shrink from accepting the fullest responsibility as to the extent of his investigations.

NECESSITY FOR INSPECTING BALANCE SHEETS.—Another general point to which it is desirable to draw attention is the danger of looking only to the Revenue Account for information as to profits. Cases are not unknown in which—the assets being taken over at an agreed valuation—the investigating Accountant has confined his attention entirely to the Revenue Account, without concerning himself with the sufficiency or otherwise of the amounts written off for depreciation and bad debts; the result being that the certified profits “as shown by the books” were greatly in excess of the profits actually earned. The Accountant who aims at something more than pocketing his fees and keeping his skin whole will not rest satisfied with that sort of investigation.

GENERAL COURSE OF PROCEDURE.—Assuming that the Accountant is about to commence an investigation into the profits of a manufacturing or trading concern during the past three (or more) years, with a view to its being purchased by a joint-stock company; the land, buildings, plant, and stock-in-trade being specially valued for that purpose by an independent valuer: assuming further that the accounts have been continuously audited by a firm of Chartered Accountants, who are satisfied as to their correctness, the question arises, What special points will the investigating

Accountant require to examine which do not arise in the ordinary course of a regular audit ?

Taking first the several Revenue Accounts, he will compare these with each other, and see whether or no they indicate a steady or consistent condition of affairs, whether the turnover fluctuates materially, and whether increasing, at a standstill, or diminishing ; whether the percentage of gross profit is fairly constant, and such as is usually earned in such undertakings ; and whether the percentages of expenses and net profit to gross turnover are reasonably steady. A marked reduction of expenses during the last year must be viewed with the greatest suspicion, for such reduction, if excessive and not *bonâ fide*, may have a very serious effect upon the future prospects of the undertaking.

So far as is reasonably practicable, the Accountant must examine the *bona fides* of all sales, especially those recorded during the last few months. The prices of at least a portion should be compared with current rates, and any remarkable increase in the amount of sales or in the number of new accounts opened should be regarded with suspicion. All entries "on approval" must be disallowed, and where sales are post-dated it seems essential to make sure that they have actually gone out of stock. The entries for the next few weeks after the closing of the books should be carefully scanned, and if they show an exceptionally large number of returns, or an exceptionally small amount of sales, he must draw his own conclusions as to the *bona fides* of such entries. In dealing with the question of consignments, he must remember that the goods have probably been invoiced out at selling prices, while the unsold balance can only be allowed for in the accounts at cost price (*plus* expenses) at most. Another point which must not be lost sight of is the question of travellers' commission : care must be taken to charge up commission upon all sales that are included in the accounts. Due allowance must also be made for all outstanding discounts ; and empties

which are returnable, but not yet returned, cannot safely be taken credit for at the full price charged.

With regard to the purchases, the problem is similar to the sales, but somewhat simpler, because the Accountant can usually get hold of the creditor's statements. It is, however, very necessary to be on one's guard against the omission of post-dated invoices when the goods have actually gone into stock.

Where reliable Stock Accounts and Cost Accounts have been kept, there exists a very valuable corroboration of the contents of the Trading Account; but where these cannot be obtained, the Accountant must do his best with the material available.

It is especially important that the various stocktakings should be conducted upon similar lines—*i.e.*, they should be based upon the same scale of prices, due allowance being made for the depreciation of articles no longer in fashion, or in small quantities, or "out" sizes.

If the various stock-lists have been prepared upon different scales of prices, they must be recast upon a uniform method, as any such difference may very materially alter the profits shown by the accounts. The valuation of the stock-in-trade made by the valuer should be compared with the vendor's stock-list, and if there is any material difference between the two, the Accountant must not fail to examine the effect of such difference upon the accounts. Thus, supposing he arrives at the conclusion that, throughout (say) the past three years, the stock has been consistently over-valued, say, 15 per cent., and supposing the stock is £10,000 heavier at the present time than it was three years ago, then during those three years the net profits will have been over-stated £1,500, or (say) £500 a year, which is a material difference when one comes to pay eight or ten years' purchase for a goodwill.

When the stock consists of such articles as cotton, iron, grain, lead, &c., which have a definite but unstable market

value, the question of the legitimacy of profits arising from such alterations in value as may have occurred is a consideration of no slight importance. This is a point upon which the author would rather not express too decided a view at the present time, but it is his opinion that (1) no profit should be taken credit for upon the rise in value of unsold stock, although Revenue must be debited with the contingent loss arising from any fall; (2) no profit should be included as part of the trading or manufacturing profits that has arisen out of a "gamble" pure and simple, but that gambling losses cannot safely be ignored; (3) where any material portion of the profits has arisen from favourable fluctuations of value—as opposed to true commercial profits—it is very desirable that the two sources of profit should be distinguished in the Accountant's report.

If there are any further items to the credit of the Profit and Loss Account, he will require to see that the profit has been actually netted, and that it is fairly incidental to the business of the undertaking. Even then, however, a purely exceptional source of profit (*e.g.*, the fact that an important exhibition had been held in that particular industry, or an altogether exceptional contract executed) should always be specially noted in the report.

Another point of no slight importance may be mentioned here, although it does not immediately arise from the preceding considerations. Where the undertaking is of such a nature that it cannot be advantageously carried on except in the present premises, the Accountant should satisfy himself that those premises will be conveyed to the company for a reasonable term. No sensible man would buy the goodwill of a hotel unless he could get a long lease, if not the freehold, of the hotel premises; while the goodwill of a music-hall held on a yearly tenancy would not usually be considered a good investment. If the lease to be granted to the company is at an increased rental, he must on no account forget to mention the fact.

Turning now to the expenses debited to Profit and Loss Account, the Accountant will require to satisfy himself that every legitimate expense has been actually included. The ordinary current expenses present no especial difficulty ; if the accounts for the past three years, or more, are available they will show these fairly well, while a study of the accounts since the date of the last Balance Sheet will probably disclose any outstanding liabilities that have been improperly omitted. Attention has already been called to the danger of a *malá fide* ruinous curtailment of expenses, so there is no occasion to again dwell upon that point.

There remain now the questions of Bad Debts, Repairs and Renewals, and Depreciation. For the purpose of dealing with these points the Accountant must refer to the Balance Sheets, as well as the Profit and Loss Accounts ; and, inasmuch as he is no longer in the realm of cut-and-dried facts, he must use the greatest amount of circumspection in arriving at his ultimate opinion.

In dealing with Bad Debts, the circumstance that he is dealing with at least three years' accounts will help him to a certain extent, for it will enable him to strike an average, and he can compare that average with what his experience teaches him to be the average usually obtaining with similar classes of undertakings. Again, the book debts of the first year, at least, are almost certain to be either collected or else written off before the end of the third year, and he can compare the percentage of the first year's actual bad debts upon its sales with the percentage written off each year. Such a comparison is of necessity only tentative, but it is useful so far as it goes. Then he can carefully examine the last schedule of book debts ; the chances are that he will know a very appreciable proportion of the names there set down, and if he finds that the schedule contains names that some of his other clients look upon as bad or doubtful, he must draw his conclusions accordingly, to the best of his judgment. In any case, and under all circumstances, he will require to satisfy himself that

a sufficient provision for bad and doubtful debts has been debited to Revenue.

With regard to the question of Depreciation, his position is, perhaps, a little more difficult. Speaking generally, if the values set forth in the Balance Sheet submitted to him exceed the amount of the valuer's estimate, he may add such difference to the amount of the depreciation debited to Revenue during the period under review. The method is not infallible, however, for the valuation at the commencement of the period may have been too high—in which case he will be charging an undue amount against the profits of the current period; or it may have been too low—in which case he will not have charged enough. There are, however, normal rates of depreciation which may be used to verify results, and previous experience, combined with sound judgment, will probably keep him from going very far wrong. Repairs should in all cases be charged up to Revenue, but actual renewals need not be, provided *due* allowance has been made for Depreciation.

If part of the assets taken over consists of shares in other companies, care must be taken to see that these are included in the accounts at their proper value. Where shares (perhaps unquoted shares) have been received in payment of book debts, especial attention is necessary, as the trading results are directly affected. Under no circumstances should Revenue be credited with more than the normal value of the work done until the shares have been actually sold, and if the profits realised on such shares form any appreciable portion of the total profits the Accountant should mention the fact in his report.

Where patents form part of the proposed purchase, and where such patents have not been submitted to a specialist for valuation, the Accountant should make it his business to see—so far as possible—that the inventions purchased are actually protected. In a recent case, a so-called patent that had been purchased by the original proprietors of the undertaking in perfect good faith was not really patented at all.

ADJUSTMENTS IN PROFITS.—For the purpose of a certificate attached to the prospectus of a new company it is usual to make certain adjustments in the statements of profits which would not ordinarily appear in the accounts of a going concern. This arises out of the difference between an investigation and an audit, the former being primarily with a view to verifying the Revenue Account (and so certifying the *normal* profit of the undertaking), while the latter is—speaking generally—confined to a verification of the present position of affairs, as shown by the Balance Sheet. In order to avoid any possibility of misconception, however, it is well to invariably state what adjustments have been made in connection with profits which would not be usual in the case of a going concern.

These adjustments would, in all ordinary cases, include the amounts paid for Income Tax, Interest on Capital, Interest on Loans, and Partners' Salaries, which may all properly be added to the net profits, provided the fact that they have been added is clearly stated. There are, however, other points which are possibly more debatable, and which will now be considered.

DEPRECIATION.—Under normal circumstances a certification as to net profits would naturally assume that a reasonable amount had been written off such profits in respect of the Depreciation of all assets necessary for the purpose of carrying on the business. It sometimes happens, however (especially where a large number of retail concerns are amalgamated, for the purpose of forming one large company), that the accounts which have to be investigated are incomplete, and that no reliable information can be obtained as to the actual value of the assets upon which Depreciation ought properly to be charged; while it may be added that the normal Depreciation would naturally to a large extent be based upon the actual cost of such assets to the present proprietors, whereas the Depreciation which will have to be charged by the proposed company in the future will of necessity have to be based upon the amount which that company actually pays for the assets in

question. Under these circumstances—and under all other circumstances where the same conditions apply—it is not merely difficult to assess the actual rate of Depreciation, but sometimes actually misleading to deal with it, even where it can be assessed. That being so, it is thought better, where these conditions apply, to certify the amount of profits which have been earned *without* any provision whatever for Depreciation, leaving the assessment of the amount necessary to provide for this contingency to those who may be interested in the matter.

CASH DISCOUNTS.—Where the concern in question has hitherto been hampered by want of capital, and has therefore not been able to take full advantage of the cash discounts offered, it is permissible, where the scheme of the proposed company provides for sufficient working capital, to take credit for the maximum cash discounts that might have been obtained, had ample working capital been employed; but advantage should never be taken of this suggestion without fully explaining the fact that credit is being taken for profits which in point of fact have not been actually realised in the past.

EXCEPTIONAL LOSSES AND PROFITS.—It has already been indicated that the main object of any investigation is to arrive at the normal profits of an undertaking; and, that being so, it is important that any exceptional sources of profit should be excluded, while *per contra* it is permissible that wholly exceptional sources of loss should be excluded. It is very difficult to define exhaustively either profits or losses coming under this category, but the following may be included.

EXCEPTIONAL LOSSES.—Losses not covered by insurance arising through fire, accidents to employees, or defalcations; provided a sufficient charge against profits is made to cover the amount which such insurance would have cost. Losses arising through actions at law not altogether incidental to the carrying on of the business, as, for instance, through breach of contract, infringements of patent, &c.; but, if the losses arising from these causes are excluded, it is essential that what-

ever profits may have been earned in connection with the subject-matter of the action should be also excluded, unless the litigation resulted in favour of the proprietors of the business being investigated.

Under the heading of EXCEPTIONAL PROFITS which ought to be excluded may be classified all such transactions as it is not reasonable in the ordinary course of events to anticipate will frequently *recur* in the carrying on of the existing business upon ordinary lines. It is naturally impossible to deal exhaustively with this class of item, but the following headings may be mentioned :—

- (1) Any profit received from a local authority or railway, by way of compensation for compulsory removal of the business premises.
- (2) Any profit received from an insurance company in respect of a risk covered by a policy of insurance.
- (3) Any profit received in connection with the sale of a portion of the undertaking, as, for instance, the sale of a patent, or of certain limited rights to work a patent, or of any fixed assets that may have been acquired for the purpose of working any portion of the concern in question, whether that department may since have been abandoned or not.

GENERALLY in matters of this description there is always a temptation to emphasise the saving which may be effected in the future by more skilful management, and by the economy which might reasonably be expected to result from the amalgamation of several concerns. These, however, are matters which, it is submitted, ought not to form the basis of any Accountant's certificate as to profits. Such certificates should be rigidly based upon facts, and although certain adjustments, as already indicated, may be desirable (and even necessary), so that a correct impression of these facts may be gathered, in view of the altered conditions which it is expected will obtain under a new company, under no circumstances

whatever should the certificate as to profits degenerate into anything which could possibly be described as an estimate, or a guess of what may under certain circumstances be expected to happen in the future.

CONCLUSION.—By this time the Accountant will have arrived at an opinion as to the amount of profits ordinarily earned by the undertaking he is investigating, but his work does not quite end here. As Mr. J. A. MOLLESON expressed it, when giving evidence in the case already quoted, “an Accountant pursuing an investigation that would be useful would wish to analyse the accounts.” Not only is it thought that such a course is most desirable as a safeguard against fraud (where a regular and satisfactory audit does not practically remove this contingency from the sphere of possibilities), but it is also extremely valuable for the purpose indicated by Mr. RICHARD BROWN, in the same case, of revealing the general nature of the business under review.

The Accountant will now have collected sufficient data to enable him to form a general impression of the business under review. He will have had ample opportunity to study the general mode upon which the business is conducted, and he will have formed his own opinion of the *personnel* of the management; he will have ascertained the amount of capital required to conduct the business upon its present lines, and have formed his own opinion as to the scope it offers for an increased capital (if such a thing be contemplated); he will have ascertained how far the continued success of the undertaking depends upon: (*a*) successful competition; (*b*) the continuance of a monopoly; and (*c*) the caprice of public demand; and have formed his own opinion concerning their continuance. In a word, he will be able to gauge the probable success of the venture. The point now to be considered is how far, if at all, his personal opinion upon these points should influence his report.

If it be conceded that the object of the Accountant's investigation is to supply the place of an independent examination

by each proposed shareholder (as the object of a professional audit is to supersede and supply the place of a personal examination by each proprietor) it must be admitted that these opinions are entitled to some expression. Yet the expression of personal opinions should be cautious and not dogmatical, and should be very clearly separated—where expressed at all—from professional opinions given, as experts, in matters of account; and further, it should never degenerate into either estimates or prophecies. It is very difficult to lay down any general rules upon this point; but, so long as the question is considered upon its merits in each particular case, the Accountant will probably not get far wrong.

The question may very possibly be raised that the Accountant who pursues the course here advocated is not likely to enjoy a very extensive investigating practice. It is thought that this conclusion offers an injustice to company promoters as a class. The profession of a company promoter is a mixed one, doubtless, but the black sheep—although naturally the most notorious—are decidedly in the minority, and there are very many promoters who would thoroughly appreciate a greater strictness in investigations, which could not fail to strengthen the confidence of the public in joint-stock enterprise as an advantageous mode of investment.

CHAPTER XII.

INCOME TAX.

It is neither necessary nor practicable that any detailed consideration of so important a subject as income-tax should be undertaken in this work ; but it so frequently happens that Auditors—both of private traders and of public companies—are asked to assist their clients in connection with assessments and appeals, that the present work would not be complete without some reference to the law and practice relating to this subject. An outline of the incidence of income-tax is therefore appended, but those who desire a more complete exposition upon the matter would do well to consult MURRAY & CARTER'S *Guide to Income Tax Practice*, or DOWELL'S *The Acts relating to Income Tax*.

CLASSES OF INCOME ASSESSABLE.—Section 2 of the Income Tax Act 1853 divides the classes of income assessable to taxation under five headings, as follows:—

Schedule A, relating to property in lands and buildings.

Schedule B, to the occupation of such lands and buildings by farmers and the like.

Schedule C, to interest and dividends payable out of the public funds of the United Kingdom, the Colonies, or any foreign State.

Schedule D, to profits accruing to a person in the United Kingdom from a trade, business, or other occupation, whether carried on in the United Kingdom or elsewhere.

(This schedule also includes interest on money and other annual profits, not included in any other schedule.)

Schedule E, relating to annuities, salaries, &c., payable out of the public revenue or by public companies.

Of these Schedule "D" is by far the most important, but it is proposed to deal shortly with each class of assessment in the first instance, and then revert to Schedule "D" in further detail.

Schedule "A."—The tax collected under this schedule is also known as the "Landlords' Property Tax." It is based upon the annual value of the lands or premises as the case may be, subject, since the passing of the Finance Act 1894, to the deduction of one-sixth in the case of houses (excluding farmhouses), and to a reduction of one-eighth in the case of lands, including farmhouses, provided, in each case, that the cost of repairs is borne by the owner. The tax is actually collected from the tenant, but may be deducted by him from his rent when paying the same over to the landlord. It is important to remember this, as it has been decided that where a tenant pays tax under Schedule "A," and inadvertently omits to deduct it when making the *next* payment of rent due, he cannot afterwards recover the amount as "money paid for the use of the landlord." The usual basis of the assessment under Schedule "A" is the poor law valuation; but this is by no means binding upon the Commissioners, although it is the custom to adopt the poor law figures when the valuation is made throughout on the full annual value of the property.

Schedule "B" is the tax levied on the occupiers of agricultural lands, nursery gardens, &c., being an estimate of the profits earned by them, based upon the rental value of the lands held. The rate of tax under this schedule is one-third of that charged under the other schedules, subject to a deduction not exceeding one-eighth of the annual value for repairs.

The Act of 1887 further provides that anyone assessable under Schedule "B" may, before assessment, elect to be assessed under Schedule "D," should he so prefer.

Schedule "C."—The tax under this schedule is always collected at the source, and the dividends or interest coming thereunder are paid out to the various stockholders *less* income-tax. If, therefore, the total income of such stockholder from all sources is such as to entitle him to abatement or exemption, it is necessary for him to apply for a return of tax overpaid.

Schedule "D" covers all cases which are not dealt with by the other schedules. The tax hereunder is, in the words of the Act, levied "for and in respect of the annual profits or gains arising or accruing to any person residing in the United Kingdom from any kind of property whatever, whether situated in the United Kingdom or elsewhere; and for and in respect of the annual profits or gains arising or accruing to any person residing in the United Kingdom from any profession, trade, employment, or vocation, whether the same shall be respectively carried on in the United Kingdom or elsewhere; and for, and in respect of the annual profits or gains arising or accruing to any person whatever, whether a subject of His Majesty or not, although not resident within the United Kingdom, from any property whatever, or any profession, trade, employment, or vocation exercised within the United Kingdom; and for and in respect of all interest of money, annuities, and other annual profits and gains not charged by virtue of any of the other schedules." It is important to bear in mind that there is a very broad distinction between the term "annual profit or gains" as used in Section 2 of the 1853 Act, and the term "net profit," as ordinarily understood by business men. The latter term is in itself sufficiently vague, but many deductions which would be clearly proper before arriving at net profits from an Accountant's point of view are not allowed under the Income Tax Acts. This, however, is a point which is more conveniently dealt with later on.

The profits of certain undertakings are (for what reason it is not altogether clear) assessed under Schedule "A" instead of under Schedule "D," although the assessment is practically based upon the business profits earned, and not upon a

hypothetical value of the land occupied. Under this heading must be included Stone, Slate, Lime-stone and Chalk quarries, which are not assessed under Schedule "D," but are assessed under Schedule "A" at an annual value computed to be the profit of the preceding year. In the same way Coal, Tin, Lead, Copper, Mundic, Iron, and other mines are assessed under Schedule "A," on an annual value which is taken to be the average profit of the five preceding years. In this connection it is of interest to note that, in the case of *Jones v. Cwmorthen Slate Co.* (decided in 1879), it was held that where slate is obtained from the side of a hill by underground workings carried on through levels, the undertaking is to be regarded as a quarry, and not as a mine. Clearly, however this decision would not apply to metals mined out of the hill-side through levels.

The following other undertakings are assessed under Schedule "A" on the assumed annual value of their respective undertakings, computed on the profits of the year preceding the year of assessment: Ironworks, Gasworks, Salt Springs or Works, Alum Mines or Works, Waterworks, Streams of Water, Canals, Inland Navigations, Docks, Drains, and Levels, Fishings, Rights of Markets and Fairs, Tolls, Railways and other ways, Bridges, Ferries, and other concerns of a like nature.

Schedule "E" relates to the salaries, annuities, pensions or stipends received, payable by His Majesty or out of the public revenue of the United Kingdom (except annuities charged under Schedule "C"), and also the salaries of Government officials, and the directors, managers, and other officers of public companies, including Auditors. As a matter of convenience, however, it is usual in the case of Auditors' fees, where these are received by professional accountants, for them to be included in a return under Schedule "D."

WHAT ARE ASSESSABLE "PROFITS."—It has already been pointed out that there is a material distinction

between the profits assessable for income-tax and what Accountants would regard as the actual net profit of the undertaking. The following items, which would in the ordinary course be debited to the Profit and Loss Account, are disallowed for income-tax purposes :—

Partners' salaries.

Income-tax.

Disbursements or expenses not wholly or exclusively laid out for purposes of trade, &c. Under this heading many classes of expenditure which the trader might consider judicious and expedient for the extension of his business would be disallowed.

Depreciation of land, buildings, or leases. Against this it must be remembered that the *full* annual value of the premises occupied may be deducted, whether that amount or a lesser amount is actually paid; the probability, therefore, is that matters come out pretty evenly in the end in this respect.

Any annual interest or annuity, or other annual payment, payable out of profits—the duty on which may, however, be deducted from the person to whom the payment is made, so that, although paid, it is not *borne* by the person assessed.

Interest on capital.

Sums expended in the improvement of premises occupied for purposes of trade. Under ordinary circumstances these would be written off out of Revenue over a term of years, but they are not allowed as a deduction for income-tax purposes at all.

The following deductions are, however, permitted :—

Repairs of premises used for the purposes of a trade or manufacture.

A sum for the supply or repairs of implements, utensils, or articles employed, not exceeding the sum actually expended

for such purposes according to the average of three years preceding.

Bad debts, or such part thereof as shall be proved to the satisfaction of the Commissioners to be bad ; also a reserve for doubtful debts "according to their estimated valued."

"Any average loss not exceeding the actual amount of loss after adjustment."

The annual value of premises used solely for the purposes of business and not as a place of residence. In the case of business premises being also used as a place of residence such proportion of the annual value as the Commissioners may think expedient will be allowed up to, and not exceeding, two-thirds of the total value. [The effect of this provision, of course, is that when the person assessed owns the freehold, or a valuable lease, of his business premises, he is allowed, as a deduction from profits, a sum that he is not called upon to pay to anyone. *Per contra* he may not deduct ground rent.]

It may be added at this point that the cost of goods supplied by the business for the private purposes of its proprietors must not be taken as an expense of the business. As an example of this it may be stated that where a restaurant keeper lives on the premises, the Commissioners require that credit shall be taken for a reasonable allowance in respect of the food and drinks consumed by himself and his family.

A sum representing the diminished value, by reason of wear and tear, of machinery or plant. It will be seen that this differs from depreciation, in that any shrinkage of value caused by the machinery or plant becoming obsolete is not included. The amount which will be allowed is in the discretion of the Commissioners, and is usually very considerably less than would be regarded as reasonably prudent in that particular class of business, not indeed often exceeding 5 per cent.

It is the practice to allow the cost of fire insurance premiums and local rates and taxes to be deducted from profits, although neither is specially provided for in the Act.

BASIS OF ASSESSMENT.—The basis of assessment under Schedule “D” in all normal cases is the average of the profits earned during the three last completed years of trading immediately preceding the current fiscal year, which commences on the 6th April. The assessment is made in advance, and is therefore subject to modification, should the estimate eventually prove to be inaccurate; this point, however, is more conveniently dealt with at a later stage.

ABATEMENTS AND EXEMPTIONS.—The following abatements and exemptions are granted when the income derived *from all sources* is less than the prescribed amount. Therefore, under some circumstances, it is desirable that the partners of a firm should each obtain a separate assessment, rather than that the assessment should be made upon the firm. For example, a firm having three equal partners may earn an average profit of £1,200 per annum; unless a separate assessment was made for each partner the firm would, therefore, have to pay the tax upon £1,200. On the other hand, if each partner was separately assessed (and had no other sources of income) his return would be for £400, and he would, therefore, be entitled to an abatement as shown hereafter. Should the advantage have been inadvertently overlooked, however, the several partners may, of course, each apply to have refunded to him the amount of tax overpaid.

At the time of writing, incomes not exceeding £160 from all sources are exempt from income-tax. Incomes exceeding £160, and not exceeding £400, are entitled to an abatement of £160; on incomes of upwards of £400 and not exceeding £500, an abatement of £150; on incomes exceeding £500 and not exceeding £600, an abatement of £120; on incomes exceeding £600 and not exceeding £700, an abatement of £70; no abatement being allowed on incomes exceeding £700.

Another form of allowance is that premiums paid to a British office on an insurance on the life of the person assessed or his wife, not exceeding in all one-sixth of the total income

assessable, may be deducted before arriving at the amount upon which tax is payable. This benefit, however, does not operate to reduce the income for the purpose of obtaining abatement or exemption under the clauses just mentioned. For example, if the total income be £420 and £70 the annual life insurance premium, this reduces the income upon which tax has to be paid to £350; but the tax must be paid upon £200 (*i.e.*, £350 less the abatement allowed on incomes between £400 and £500), and not on £190 (*i.e.*, £350 less the abatement on incomes between £160 and £400).

For the purpose of claiming abatement or exemption the incomes of husband and wife must be aggregated. That is, their united incomes must be less than the prescribed amount to entitle them to the benefit of the concession. If, however, both husband and wife earn their respective incomes (or part of them) by actual personal endeavour, and their united income does not exceed £500 per annum, they are entitled to claim to be separately assessed.

CLASSES OF UNDERTAKINGS EXEMPT FROM INCOME TAX.—Various public bodies and charitable institutions are exempt from the operations of the Income Tax Acts, and the Auditor must, therefore, see that the tax which has been deducted from any income receivable by these bodies is applied for and returned to them. Friendly societies, trustee savings banks, and industrial and provident societies are also exempt, but building societies are not.

ON THE OTHER HAND, joint stock companies, &c., are always assessed upon the amount of their actual profits, and are not entitled to claim either abatement or exemption. The usual practice is for them to deduct income-tax from all dividends paid by them, and, of course, income-tax should in all cases be deducted from preference dividends, and from debenture and mortgage interest; and the shareholders or debenture-holders whose total income is such as to entitle them to the

benefit of exemption or abatement may apply for a return of the tax so deducted.

MODIFICATION OF ORIGINAL ASSESSMENT.—

When, at the end of the year, it is found that the amount of profits upon which income-tax has been paid is in excess of the actual profit for the period just closed, the trader is entitled to apply for a return of the tax so over-paid. In support of this application he must show the average profits earned by him during the past three years, including the year of assessment; and, if this average profit is less than the average profit upon which the assessment has been made, the difference will be refunded: this, however, is subject to the qualification that, if the profits earned during the year of assessment exceed the (revised) average profits, relief will only be granted to the extent of the difference between the latter and the original assessment. All applications for relief under this provision should be made to the Surveyor of Taxes in the district where the person assessed *resides*. *Per contra*, the income-tax authorities are entitled to make a further assessment where they are satisfied that the original assessment has been insufficient. In practice, of course, this is but rarely done; but in the case of undertakings which are being formed into limited companies, the Income-tax Surveyors sometimes take advantage of the profits disclosed by the prospectus to secure a further payment of income-tax on the past year.

RATE OF INCOME TAX.—The rate of the income-tax is settled annually by Act of Parliament. The rates during recent years have been as follow:—

From 6th April 1895 to 5th April 1900, 8d. in the £.

Do.	1900	Do.	1901, 1/-	Do.
Do.	1901	Do.	1902, 1/2	Do.
Do.	1902	Do.	1903, 1/3	Do.
Do.	1903	Do.	1904, 11d.	Do.
Do.	1904	Do.	1907, 1/-	Do.

Income-tax is accordingly deductible at the rate of One Shilling in the Pound on all payments made subsequent to the 5th April 1904 in respect of—

- (a) Dividends and Interest from the Public Funds payable on or after the 6th April 1904.
- (b) Dividends and Interest of Foreign or Colonial Government Securities, or of Foreign or Colonial Companies *entrusted to an Agent in this Country for payment here on or after the 6th April 1904*; also of like Dividends or Interest which although not entrusted to an Agent in this Country for payment are *realised in the United Kingdom on or after that date* through Bankers, Coupon Dealers, or other persons.
- (c) Interest and Annuities paid by Municipal Corporations or other Local Authorities to Creditors on Rates.
- (d) Interest and Annuities not paid or not wholly paid out of profits and gains brought into charge to Income Tax

But in respect of—

- (a) Ground Rents, &c., secured on Property charged with Income Tax;
- (b) Interest or Annuities wholly payable out of Property, Profits, or Gains charged with Income Tax;
- (c) Dividends paid out of the Profits or Gains of Public Companies in the United Kingdom,

the tax is deductible at the rate or rates in force during the period in which the same has or have been accruing—*i.e.*, in respect of any portion which accrued in the year ended 5th April 1904 at the rate of Eleven Pence in the Pound, and in respect of any portion accruing subsequent to that date at the rate of One Shilling in the Pound.

These same principles, of course, hold good in respect of changes in the income-tax rates effected in other years.

APPENDIX A.

EXTRACTS FROM STATUTES

REFERRED TO IN THE COURSE OF THIS WORK.

GENERAL.

LARCENY ACT, 1861.

24 and 25 Vict. c. 96.

Directors, &c., Fraudulently Appropriating Property.

81.—Whosoever, being a director, member, or public officer of any body corporate or public company, shall fraudulently take or apply for his own use or benefit, or for any use or purposes other than the use or purposes of such body corporate or public company, any of the property of such body corporate or public company, shall be guilty of a misdemeanour, and being convicted thereof shall be liable, at the discretion of the Court, to any of the punishments which the Court may award as hereinbefore last mentioned.

Keeping Fraudulent Accounts.

82.—Whosoever, being a director, public officer, or manager of any body corporate or public company, shall as such receive or possess himself of any of the property of such body corporate or public company otherwise than in payment of a just debt or demand, and shall, with intent to defraud, omit to make, or to cause or direct to be made, a full and true entry thereof in the books and accounts of such body corporate or public company, shall be guilty of a misdemeanour, and being convicted thereof shall be liable, at the discretion of the Court, to any of the punishments which the Court may award as hereinbefore last mentioned.

Wilfully Destroying Books, &c.

83.—Whosoever, being a director, manager, public officer, or member of any body corporate or public company, shall, with intent to defraud, destroy, alter, mutilate, or falsify any book, paper, writing, or valuable security belonging to the body corporate or public company, or make or concur in the making of any false entry or omit or concur in omitting

any material particular, in any book of account or other document, shall be guilty of a misdemeanour, and being convicted thereof shall be liable, at the discretion of the Court, to any of the punishments which the Court may award as hereinbefore last mentioned.

Publishing False Statements.

84.—Whosoever, being a director, manager, or public officer of any body corporate or public company, shall make, circulate, or publish, or concur in making, circulating, or publishing, any written statement or account which he shall know to be false in any material particular, with intent to deceive or defraud any member, shareholder, or creditor of such body corporate or public company, or with intent to induce any person to become a shareholder or partner therein, or to entrust or advance any property to such body corporate or public company, or to enter into any security for the benefit thereof, shall be guilty of a misdemeanour, and being convicted thereof shall be liable, at the discretion of the Court, to any of the punishments which the Court may award as hereinbefore last mentioned.

FALSIFICATION OF ACCOUNTS ACT, 1875.

38 and 39 Vict. c. 24.

1.—That if any clerk, officer, or servant, or any person employed or acting in the capacity of a clerk, officer, or servant, shall wilfully and with intent to defraud, destroy, alter, mutilate, or falsify any book, paper, writing, valuable security, or account which belongs to or is in the possession of his employer, or has been received by him for or on behalf of his employer, or shall wilfully, and with intent to defraud, make, or concur in making, any false entry in, or omit or alter, or concur in omitting or altering, any material particular form, or in any such book, or any document or account, then in every such case the person so offending shall be guilty of a misdemeanour, and be liable to be kept in penal servitude for a term not exceeding seven years, or to be imprisoned with or without hard labour for any term not exceeding two years.

2.—It shall be sufficient in any indictment under this Act to allege a general intent to defraud, without naming any particular person to be defrauded.

It is further declared (section 3) that "this Act shall be read as one with the Act of the twenty-fourth and twenty-fifth of her Majesty, chapter ninety-six," section 82 of which makes it a misdemeanour on the part of any director, public officer, or manager of any body corporate

or public company, who shall "as such receive or possess himself of any of the property of such body corporate or public company, otherwise than in payment of a just debt or demand, and shall, with intent to defraud, omit to make, or to cause or direct to be made, a full and true entry thereof in the books or accounts of such body corporate or public company." The following section (83) makes it a misdemeanour on the part of any such person, who shall "with intent to defraud, destroy, alter, mutilate, or falsify any book, paper, writing, or valuable security belonging to the body corporate or public company, or make, or concur in the making, of any false entry, or omit, or concur in omitting, any material particular in any book of account or other document." And section 84 makes it a similar offence on the part of any such person who "shall make, circulate, or publish, or concur in making, circulating, or publishing, any written statement or account which he shall know to be false in any material particular, with intent to deceive or defraud any member, shareholder, or creditor, of such body corporate or public company, or with intent to induce any person to become a shareholder, or partner therein, or to entrust or advance any property to such body corporate or public company, or to enter into any security for the benefit thereof."

PREVENTION OF CORRUPTION ACT, 1906.

6 Edw. VII. Ch. 34.

Be it enacted by the King's most Excellent Majesty, by and with the advice and consent of the Lords Spiritual and Temporal, and Commons, in this present Parliament assembled, and by the authority of the same as follows:—

- 1.—(1) If any agent corruptly accepts or obtains, or agrees to accept or attempts to obtain, from any person, for himself or for any other person, any gift or consideration as an inducement or reward for doing or forbearing to do, or for having after the passing of this Act done or forborne to do, any act in relation to his principal's affairs or business, or for showing or forbearing to show favour or disfavour to any person in relation to his principal's affairs or business; or

If any person corruptly gives or agrees to give or offers any gift or consideration to any agent as an inducement or reward for doing or forbearing to do, or for having after the passing of this Act done or forborne to do, any act in relation to his principal's affairs or business, or for showing or forbearing to show favour or disfavour to any person in relation to his principal's affairs or business; or

If any person knowingly gives to any agent, or if any agent knowingly uses with intent to deceive his principal, any receipt, account, or other document in respect of which the principal is interested, and which contains any statement which is false or erroneous or defective in any material particular, and which to his knowledge is intended to mislead the principal;

he shall be guilty of a misdemeanour, and shall be liable on conviction on indictment to imprisonment, with or without hard labour, for a term not exceeding two years, or to a fine not exceeding five hundred pounds, or to both such imprisonment and such fine, or on summary conviction to imprisonment, with or without hard labour, for a term not exceeding four months, or to a fine not exceeding fifty pounds, or to both such imprisonment and such fine.

(2) For the purposes of this Act the expression "consideration" includes valuable consideration of any kind; the expression "agent" includes any person employed by or acting for another; and the expression "principal" includes an employer.

(3) A person serving under the Crown or under any corporation or any municipal, borough, county, or district council, or any board of guardians, is an agent within the meaning of this Act.

2.—(1) A prosecution for an offence under this Act shall not be instituted without the consent, in England of the Attorney-General or Solicitor-General, and in Ireland of the Attorney-General or Solicitor-General for Ireland.

(2) The Vexatious Indictments Act 1859, as amended by any subsequent enactment, shall apply to offences under this Act as if they were included among the offences mentioned in Section 1 of that Act.

(3) Every information for any offence under this Act shall be upon oath.

(4) The expenses of any prosecution on indictment under this Act shall be defrayed as in cases of indictment for felony.

(5) A Court of Quarter Sessions shall not have jurisdiction to inquire of, hear, and determine prosecutions on indictments for offences under this Act.

(6) Any person aggrieved by a summary conviction under this Act may appeal to a Court of Quarter Sessions.

3.—This Act shall extend to Scotland, subject to the following modifications:—

(1) Section 2 shall not extend to Scotland:

- (2) In Scotland all offences which are punishable under this Act on summary conviction shall be prosecuted before the sheriff in manner provided by the Summary Jurisdiction (Scotland) Acts.

4.—(1) This Act may be cited as the Prevention of Corruption Act 1906.

- (2) This Act shall come into operation on the first day of January nineteen hundred and seven.

COMPANIES.

THE COMPANIES ACT, 1862.

25 and 26 Vict. c. 89.

Application of Table A.

15.—In the case of a company limited by shares, if the memorandum of association is not accompanied by articles of association, or in so far as the articles do not exclude or modify the regulations contained in the table marked "A" in the first schedule hereto, the last-mentioned regulations shall, so far as the same are applicable, be deemed to be the regulations of the company in the same manner and to the same extent as if they had been inserted in articles of association, and the articles had been duly registered.

Register of Members.

25.—Every company under this Act shall cause to be kept in one or more books a register of its members, and there shall be entered therein the following particulars:—

- (1) The names and addresses, and the occupations, if any, of the members of the company, with the addition, in the case of a company having a capital divided into shares, of a statement of the shares held by each member, distinguishing each share by its number; and of the amount paid or agreed to be considered as paid on the shares of each member:
- (2) The date at which the name of any person was entered in the register as a member:
- (3) The date at which any person ceased to be a member:

And any company acting in contravention of this section shall incur a penalty not exceeding five pounds for every day during which its default in complying with the provisions of this section continues, and every director or manager of the company who shall knowingly and wilfully authorise or permit such contravention shall incur the like penalty.

Annual List of Members.

26.—Every company under this Act, and having a capital divided into shares, shall make, once at least in every year, a list of all persons who, on the fourteenth day succeeding the day on which the ordinary general meeting, or if there is more than one ordinary meeting in each year, the first of such ordinary general meetings is held, are members of the company; and such lists shall state the names, addresses, and occupations of all the members therein mentioned, and the number of shares held by each of them, and shall contain a summary specifying the following particulars:—

- (1) The amount of the capital of the company, and the number of shares into which it is divided:
- (2) The number of shares taken from the commencement of the company up to the date of the summary:
- (3) The amount of calls made on each share:
- (4) The total amount of calls received:
- (5) The total amount of calls unpaid:
- (6) The total amount of shares forfeited:
- (7) The names, addresses, and occupations of the persons who have ceased to be members since the last list was made, and the number of shares held by each of them.

The above list and summary shall be contained in a separate part of the register, and shall be completed within seven days after such fourteenth day as is mentioned in this section, and a copy shall forthwith be forwarded to the Registrar of Joint Stock Companies.

Register of Mortgages.

43.—Every limited company under this Act shall keep a register of all mortgages and charges specifically affecting property of the company, and shall enter in such register in respect of each mortgage or charge a short description of the property mortgaged or charged, the amount of charge created, and the names of the mortgagees or persons entitled to such charge: If any property of the company is mortgaged or charged without such entry as aforesaid being made, every director, manager, or other officer of the company who knowingly and wilfully authorises or permits the omission of such entry shall incur a penalty not exceeding fifty pounds: The register of mortgages required by this section shall be open to inspection by any creditor or member of the company at all reasonable times; and if such inspection is refused, any officer of the company refusing the same, and every director and manager of the company authorising or knowingly and wilfully permitting such refusal,

shall incur a penalty not exceeding five pounds, and a further penalty not exceeding two pounds for every day during which such refusal continues; and in addition to the above penalty, as respects companies registered in *England* and *Ireland*, any Judge sitting in Chambers, or the Vice-Warden of the Stannaries in the case of companies subject to his jurisdiction, may by order compel an immediate inspection of the register.

Certain Companies to Publish Statement entered in Schedule.

44.—Every limited banking company and every insurance company, and deposit, provident, or benefit society under this Act, shall, before it commences business, and also on the first *Monday* in *February* and the first *Monday* in *August* in every year during which it carries on business, make a statement in the form marked "D" in the first schedule hereto, or as near thereto as circumstances will admit, and a copy of such statement shall be put up in a conspicuous place in the registered office of the company, and in every branch office or place where the business of the company is carried on, and if default is made in compliance with the provisions of this section the company shall be liable to a penalty not exceeding five pounds for every day during which such default continues, and every director and manager of the company who shall knowingly and wilfully authorise or permit such default shall incur the like penalty.

Every member and every creditor of any company mentioned in this section shall be entitled to a copy of the above-mentioned statement on payment of a sum not exceeding sixpence.

List of Directors to be sent to Registrar.

45.—Every company under this Act [and not having a capital divided into shares]* shall keep at its registered office a register containing the names and addresses and occupations of its directors or managers, and shall send to the Registrar of Joint Stock Companies a copy of such register, and shall, from time to time, notify to the Registrar any change that takes place in such directors or managers.

FIRST SCHEDULE.

TABLE A.

(*Applicable to Companies Registered without Special Articles prior to 1st October 1906.*)

Accounts.

78.—The directors shall cause true accounts to be kept of the stock-in-trade of the company, of the sums of money received and expended by

* Repealed by Companies Act 1900.

the company, and the matter in respect of which such receipts and expenditure takes place; and of the liabilities and credits of the company. The books of account shall be kept at the registered office of the company, and, subject to any reasonable restrictions as to the time and manner of inspecting the same that may be imposed by the company in general meeting, shall be open to the inspection of the members during the hours of business.

79.—Once at least in every year the directors shall lay before the company, in general meeting, a statement of the income and expenditure for the past year, made up to a date not more than three months before such meeting.

80.—The statement so made shall show, arranged under the most convenient heads, the amount of gross income, distinguishing the several sources from which it has been derived; and the amount of gross expenditure, distinguishing the expense of the establishment, salaries, and other like matters. Every item of expenditure fairly chargeable against the year's income shall be brought into account, so that a just balance of profit and loss may be laid before the meeting; and in cases where any item of expenditure which may in fairness be distributed over several years has been incurred in any one year, the whole amount of such item shall be stated, with the addition of the reasons why only a portion of such expenditure is charged against the income of the year.

81.—A Balance Sheet shall be made out in every year, and laid before the company in general meeting, and such Balance Sheet shall contain a summary of the property and liabilities of the company arranged under the heads appearing in the form annexed to this table, or as near thereto as circumstances admit.

82.—A printed copy of such Balance Sheet shall, seven days previously to such meeting, be served on every member, in the manner in which notices are hereinafter directed to be served.

Audit.

83.—Once at least in every year the accounts of the company shall be examined, and the correctness of the Balance Sheet ascertained, by one or more Auditor or Auditors.

84.—The first Auditors shall be appointed by the directors. Subsequent Auditors shall be appointed by the company in general meeting.

85.—If one Auditor only is appointed all the provisions herein contained relating to Auditors shall apply to him.

86.—The Auditors may be members of the company; but no person is eligible as an Auditor who is interested otherwise than as a member

in any transaction of the company ; and no director or other officer of the company is eligible during his continuance in office.

87.—The election of Auditors shall be made by the company at their ordinary meeting in each year.

88.—The remuneration of the first Auditors shall be fixed by the directors ; that of subsequent Auditors shall be fixed by the company in general meeting.

89.—Any Auditor shall be re-eligible on his quitting office.

90.—If any casual vacancy occurs in the office of any Auditor appointed by the company, the directors shall forthwith call an extraordinary general meeting for the purpose of supplying the same.

91.—If no election of Auditors is made in manner aforesaid, the Board of Trade may, on the application of not less than five members of the company, appoint an Auditor for the current year, and fix the remuneration to be paid to him by the company for his services.

92.—Every Auditor shall be supplied with a copy of the Balance Sheet, and it shall be his duty to examine the same, with the accounts and vouchers relating thereto.

93.—Every Auditor shall have a list delivered to him of all books kept by the company, and shall at all reasonable times have access to the books and accounts of the company. He may, at the expense of the company, employ accountants or other persons to assist him in investigating such accounts, and he may in relation to such accounts examine the directors or any other officer of the company.

94.—The Auditors shall make a report to the members upon the Balance Sheet and accounts, and in every such report they shall state whether, in their opinion, the Balance Sheet is a full and fair Balance Sheet, containing the particulars required by these regulations, and properly drawn up so as to exhibit a true and correct view of the state of the company's affairs : and in case they have called for explanations or information from the directors, whether such explanations or information have been given by the directors, and whether they have been satisfactory : and such report shall be read, together with the report of the directors, at the ordinary meeting.

Dr.

Cr.

BALANCE SHEET of the

Co., made up to

19 .

CAPITAL AND LIABILITIES.

PROPERTY AND ASSETS.

I. CAPITAL.	Showing:	£ s d	III. Property held by the Company.	Showing:	£ s d
1. The number of Shares	The amount paid per Share .. ..	.. ..	7. Immovable Property, distinguishing:	(a) Freehold Land .. ..	.. ..
2. The amount paid per Share	3. If any arrears of Calls, the nature of the .. ..	.. ..	(b) Buildings	(c) Leasehold .. ..	.. ..
3. If any arrears of Calls, the nature of the	4. The particulars of any forfeited Shares .. ..	.. ..	8. Movable Property, distinguishing:	(d) Stock-in-Trade .. ..	.. ..
4. The particulars of any forfeited Shares	5. The amount of Loans on Mortgages or .. ..	.. ..	Debenture Bonds	(e) Plant .. ..	.. ..
5. The amount of Loans on Mortgages or	6. The amount of Debts owing by the Com- .. ..	.. ..	pany, distinguishing:	The cost to be stated with deductions .. ..	.. ..
6. The amount of Debts owing by the Com-	(a) Debts for which acceptances have .. ..	.. ..	been given	for deterioration in value as charged to .. ..	.. ..
7. The amount of Debts owing by the Com-	(b) Debts to Tradesmen for Supplies .. ..	.. ..	of Stock-in-Trade or other articles	the Reserve Fund or Profit and Loss.	.. ..
8. The amount of Debts owing by the Com-	(c) Debts for Law Expenses .. ..	.. ..	(d) Debts for Interest on Debentures	IV. DEBTS OW- .. ..	.. ..
9. The amount of Debts owing by the Com-	(e) Unclaimed Dividends .. ..	.. ..	(f) Debts not enumerated above	ing to the .. ..	.. ..
10. The amount of Debts owing by the Com-	VI. RESERVE .. ..	.. ..	FUND.	Company.	.. ..
11. The amount of Debts owing by the Com-	The amount set aside from Profits to meet .. ..	.. ..	Contingencies.. ..	Company.	.. ..
12. The amount of Debts owing by the Com-	Showing:	.. ..	VII. PROFIT &	V. CASH AND .. ..	.. ..
13. The amount of Debts owing by the Com-	The disposable Balance for payment of .. ..	.. ..	Loss.	INVESTMENTS.	.. ..
14. The amount of Debts owing by the Com-	Dividends, &c. .. ..	.. ..	Claims against the Company not acknow-	Showing: .. ..	.. ..
15. The amount of Debts owing by the Com-	ledged as Debts .. ..	.. ..	Moneys for which the Company is con-	The nature of Investment and rate of .. ..	.. ..
16. The amount of Debts owing by the Com-	tingently liable .. ..	.. ..	Interest	The amount of Cash, where lodged, and .. ..	.. ..
17. The amount of Debts owing by the Com-	if bearing Interest .. ..	.. ..	.. ..	.. ..	.. ..

FORM D.

FORM OF STATEMENT referred to in Part III. of the Act.

*The capital of the company is divided into
shares of each.

The number of shares issued is .

Calls to the amount of pounds per share have been made
under which the sum of pounds has been received.

The liabilities of the company on the 1st day of January (or July)
were—

Debts owing to sundry persons by the company.

On judgment, £

On specialty, £

On notes or bills, £

On simple contracts, £

On estimated liabilities, £

The assets of the company on that day were—

Government securities [*stating them*], £

Bills of exchange and promissory notes, £

Cash at the bankers, £

Other securities, £

* If the company has no capital divided into shares, the portion of the statement relating to capital and shares must be omitted.

REVISED "TABLE A."

(*Applicable to all Companies registered without Special Articles on or after
1st October 1906.*)

Preliminary.

1.—In these regulations, unless the context otherwise requires, expressions defined in the Companies Acts 1862 to 1900, or any statutory modification thereof in force at the date at which these regulations become binding on the company, shall have the meanings so defined; and words importing the singular number only shall include the plural

number, and *vice versa*, and words importing the masculine gender shall include the feminine, and words importing persons shall include corporations.

Shares.

3.—Subject to the provisions, if any, in that behalf of the memorandum of association of the company, and without prejudice to any special rights previously conferred on the holders of existing shares in the company, any share in the company may be issued with such preferred, deferred, or other special rights, or such restrictions, whether in regard to dividend, voting, return of capital, or otherwise, as the company may from time to time by special resolution determine.

4.—If at any time the capital is divided into different classes of shares, the rights attached to any class (unless otherwise provided by the terms of issue of the shares of that class) may be varied with the consent in writing of the holders of three-fourths of the issued shares of that class, or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of the shares of the class. To every such separate general meeting the provisions of these regulations relating to general meetings shall *mutatis mutandis* apply, but so that the necessary quorum shall be two persons at least holding or representing by proxy one-third of the issued shares of the class.

Forfeiture of Shares.

24.—If a member fails to pay any call or instalment of a call on the day appointed for payment thereof, the directors may, at any time thereafter during such time as any part of such call or instalment remains unpaid, serve a notice on him requiring payment of so much of the call or instalment as is unpaid, together with any interest which may have accrued.

25.—The notice shall name a further day (not earlier than the expiration of fourteen days from the date of the notice) on or before which the payment required by the notice is to be made, and shall state that in the event of non-payment at or before the time appointed the shares in respect of which the call was made will be liable to be forfeited.

26.—If the requisitions of any such notice as aforesaid are not complied with, any share in respect of which the notice has been given may at any time thereafter, before the payment required by the notice has been made, be forfeited by a resolution of the directors to that effect.

27.—A forfeited share may be sold or otherwise disposed of on such terms and in such manner as the directors think fit, and at any time

before a sale or disposition the forfeiture may be cancelled on such terms as the directors think fit.

28.—A person whose shares have been forfeited shall cease to be a member in respect of the forfeited shares, but shall, notwithstanding, remain liable to pay to the company all moneys which, at the date of forfeiture, were presently payable by him to the company in respect of the shares, but his liability shall cease if and when the company shall have received payment in full of the nominal amount of the shares.

29.—A statutory declaration in writing that the declarant is a director of the company, and that a share in the company has been duly forfeited on a date stated in the declaration, shall be conclusive evidence of the facts therein stated as against all persons claiming to be entitled to the share, and such declaration, and the receipt of the company for the consideration, if any, given for the share on the sale or disposition thereof, shall constitute a good title to such share, and the person to whom the share is sold or disposed of shall be registered as the holder of the share and shall not be bound to see to the application of the purchase-money, if any, nor shall his title to the share be affected by any irregularity or invalidity in the proceedings in reference to the forfeiture, sale, or disposal of the share.

30.—The provisions of these regulations as to forfeiture shall apply in the case of non-payment of any sum which, by the terms of issue of a share, becomes payable at a fixed time, whether on account of the amount of the share or by way of premium, as if the same had been payable by virtue of a call duly made and notified.

Alteration of Capital.

41.—The directors may, with the sanction of an extraordinary resolution of the company, increase the capital by such sum, to be divided into shares of such amount, as the resolution shall prescribe.

42.—Subject to any direction to the contrary that may be given by the resolution sanctioning the increase of capital, all new shares shall, before issue, be offered to such persons as at the date of the offer are entitled to receive notices from the company of general meetings in proportion, as nearly as the circumstances admit, to the amount of the existing shares to which they are entitled. Such offer shall be made by notice specifying the number of shares offered, and limiting a time within which the offer, if not accepted, will be deemed to be declined, and after the expiration of such time, or on the receipt of an intimation from the person to whom the offer is made that he declines to accept the shares offered, the directors may dispose of the same in such manner

as they think most beneficial to the company. The directors may likewise so dispose of any new shares which (by reason of the ratio which the new shares bear to shares held by persons entitled to an offer of new shares) cannot, in the opinion of the directors, be conveniently offered under this article.

43.—The new shares shall be subject to the same provisions with reference to the payment of calls, lien, transfer, transmission, forfeiture and otherwise as the shares in the original capital.

44.—The company may, by special resolution :—

- (a) Consolidate and divide its capital into shares of larger amount than its existing shares.
- (b) By sub-division of its existing shares, or any of them, divide the whole, or any part, of its capital into shares of smaller amount than is fixed by the memorandum of association, subject, nevertheless, to the proviso contained in the Companies Act, 1867, Section 21.
- (c) Cancel any shares which, at the date of the passing of the resolution, have not been taken or agreed to be taken by any person.
- (d) Reduce its capital in any manner and with, and subject to, any incident authorised, and consent required, by law.

Disqualifications of Directors.

77.—The office of director shall be vacated :—

If he ceases to be a director by virtue of the Companies Act, 1900, Section 3.

If he holds any other office of profit under the company except that of managing director or manager.

If he becomes bankrupt.

If he is found lunatic or becomes of unsound mind.

If he is concerned or participates in the profits of any contract with the company.

But the above rules shall be subject to the following exceptions :—
That no director shall vacate his office by reason of his being a member of any company which has entered into contracts with or done any work for the company of which he is director : nevertheless he shall not vote in respect of such contract or work : and if he does so vote his vote shall not be counted.

Dividends and Reserve.

95.—The company in general meeting may declare dividends, but no dividend shall exceed the amount recommended by the directors.

96.—The directors may from time to time pay to the members such interim dividends as appear to the directors to be justified by the profits of the company.

97.—No dividend shall be paid otherwise than out of profits.

98.—Subject to the rights of persons, if any, entitled to shares with special rights as to dividend, all dividends shall be declared and paid according to the amounts paid on the shares, but if and so long as nothing is paid up on any of the shares in the company dividends may be declared and paid according to the amounts of the shares. No amount paid on a share in advance of calls shall, while carrying interest, be treated for the purposes of this article as paid on the share.

99.—The directors may, before recommending any dividend, set aside out of the profits of the company such sums as they think proper as a reserve or reserves which shall, at the discretion of the directors, be applicable for meeting contingencies, or for equalising dividends, or for any other purpose to which the profits of the company may be properly applied, and pending such application may, at the like discretion, either be employed in the business of the company or be invested in such investments (other than shares of the company) as the directors may from time to time think fit.

100.—If several persons are registered as joint holders of any share any one of them may give effectual receipts for any dividend payable on the share.

101.—Notice of any dividend that may have been declared shall be given in manner hereinafter mentioned to the persons entitled to share therein.

102.—No dividend shall bear interest against the company.

Accounts.

103.—The directors shall cause true accounts to be kept:—

Of the sums of money received and expended by the company and the matter in respect of which such receipt and expenditure takes place; and

Of the assets and liabilities of the company.

104.—The books of account shall be kept at the registered office of the company, or at such other place or places as the directors think fit, and shall always be open to the inspection of the directors.

105.—The directors shall from time to time determine whether and to what extent and at what times and places and under what conditions or regulations the accounts and books of the company or any of them shall be open to the inspection of members not being directors, and no member (not being a director) shall have any right of inspecting any account or book or document of the company except as conferred by statute or authorised by the directors or by the company in general meeting.

106.—Once at least in every year the directors shall lay before the company in general meeting a Profit and Loss Account for the period since the preceding account or (in the case of the first account) since the incorporation of the company, made up to a date not more than six months before such meeting.

107.—A Balance Sheet shall be made out in every year, and laid before the company in general meeting made up to a date not more than six months before such meeting. The Balance Sheet shall be accompanied by a report of the directors as to the state of the company's affairs, and the amount which they recommend to be paid by way of dividend, and the amount, if any, which they propose to carry to a reserve fund.

108.—A copy of such Balance Sheet and report shall, seven days previously to the meeting, be sent to the persons entitled to receive notices of general meetings in the manner in which notices are to be given hereunder.

Audit.

109.—Auditors shall be appointed and their duties regulated in accordance with the Companies Act 1900, Sections 21, 22, and 23, or any statutory modification thereof for the time being in force.

THE COMPANIES ACT, 1879.

42 and 43 Vict. c. 76.

4.—Subject as in this Act mentioned, any company registered before or after the passing of this Act as an unlimited company may register under the Companies Acts 1862 to 1879, as a limited company, or any company already registered as a limited company may re-register under the provisions of this Act.

Audit of Accounts of Banking Companies.

7.—(1) Once at least in every year the accounts of every banking company registered after the passing of this Act as a limited company shall be examined by an Auditor or Auditors, who shall be elected annually by the company in general meeting.

(2) A director or officer of the company shall not be capable of being elected Auditor of such company.

(3) An Auditor on quitting office shall be re-eligible.

(4) If any casual vacancy occurs in the office of any Auditor, the surviving Auditor or Auditors (if any) may act, but if there is no surviving Auditor, the directors shall forthwith call an extraordinary general meeting for the purpose of supplying the vacancy or vacancies in the auditorship.

(5) Every Auditor shall have a list delivered to him of all books kept by the company, and shall at all reasonable times have access to the books and accounts of the company; and any Auditor may, in relation to such books and accounts, examine the directors or any other officer of the company: Provided that if a banking company has branch banks beyond the limits of Europe, it shall be sufficient if the Auditor is allowed access to such copies of and extracts from the books and accounts of any such branch as may have been transmitted to the head office of the banking company in the United Kingdom.

Report of Auditors.

(6) The Auditor or Auditors shall make a report to the members on the accounts examined by him or them, and on every Balance Sheet laid before the company in general meeting during his or their tenure of office; and in every such report shall state whether, in his or their opinion, the Balance Sheet referred to in the report is a full and fair Balance Sheet properly drawn up, so as to exhibit a true and correct view of the state of the company's affairs, as shown by the books of the company; and such report shall be read before the company in general meeting.

(7) The remuneration of the Auditor or Auditors shall be fixed by the general meeting appointing such Auditor or Auditors, and shall be paid by the company.

8.—Every Balance Sheet submitted to the annual or other meeting of the members of every banking company registered after the passing of this Act as a limited company shall be signed by the Auditor or Auditors, and by the secretary or manager (if any), and by the directors of the company, or three of such directors at the least.

COMPANIES (WINDING-UP) ACT, 1890.

*53 and 54 Vict. c. 63.**Report by Official Receiver and Proceedings thereon.*

8.—(1) Where the Court has made an order for winding-up a company the Official Receiver shall, as soon as practicable after receipt of the statement of the company's affairs, submit a preliminary report to the Court—

- (a) As to the amount of capital issued, subscribed, and paid up, and the estimated amount of assets and liabilities; and
- (b) If the company has failed, as to the causes of the failure; and
- (c) Whether in his opinion further inquiry is desirable as to any matter relating to the promotion, formation, or failure of the company, or the conduct of the business thereof.

(2) The Official Receiver may also, if he thinks fit, make a further report, or further reports, stating the manner in which the company was formed, and whether in his opinion any fraud has been committed by any person in the promotion or formation of the company, or by any director or other officer of the company in relation to the company since the formation thereof, and any other matters which, in his opinion, it is desirable to bring to the notice of the Court.

(3) The Court may, after consideration of any such report, direct that any person who has taken any part in the promotion or formation of the company, or has been a director or officer of the company, shall attend before the Court on a day appointed by the Court for that purpose, and be publicly examined as to the promotion or formation of the company, or as to the conduct of the business of the company, or as to his conduct and dealings as director or officer of the company.

(4) The Official Receiver shall take part in the examination, and for that purpose may, if specially authorised by the Board of Trade in that behalf, employ a solicitor with or without counsel.

(5) The liquidator, where the Official Receiver is not the liquidator, and any creditor or contributory of the company, may also take part in the examination, either personally or by solicitor or counsel.

(6) The Court may put such questions to the person examined as to the Court may seem expedient.

(7) The person examined shall be examined on oath, and it shall be his duty to answer all such questions as the Court may put or allow to be put to him. The person examined shall at his own cost, prior to such examination, be furnished with a copy of the Official Receiver's report and shall also at his own cost be entitled to employ at such examination

a solicitor with or without counsel, who shall be at liberty to put such questions to the person examined as the Court may deem just, for the purpose of enabling that person to explain or qualify any answer given by him. Provided always, that if such person is, in the opinion of the Court, exculpated from any charges made or suggested against him, the Court may allow him such costs as the Court in its discretion may think fit. Notes of the examination shall be taken down in writing, and shall be read over to or by, and signed by, the person examined, and may thereafter be used in evidence against him. They shall also be open to the inspection of any creditor or contributory of the company at all reasonable times.

(8) The Court may, if it thinks fit, adjourn the examination from time to time.

(9) A public examination under this section may, if the Court so directs, and subject to general rules, be held before any Judge of County Courts, or before any officer of the Supreme Court, being an official referee, master, registrar of bankruptcy, or chief clerk, or before any district registrar in the High Court named for the purpose by the Lord Chancellor, or in the case of companies being wound up by a Palatine Court, before a registrar of that Court, and the powers of the Court under sub-sections six, seven, and eight of this section may (except as to costs) be exercised by the person before whom the examination is held.

Damages for Misfeasance.

10.—(1) Where in the course of the winding-up of a company under the Companies Act it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager, liquidator, or other officer of the company, has misapplied or retained or become liable or accountable for any moneys or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may, on the application of the Official Receiver, or the liquidator of the company, or of any creditor or contributory of the company, examine into the conduct of such promoter, director, manager, liquidator, or other officer of the company, and compel him to repay any moneys or restore any property so misapplied or retained, or for which he has become liable, or accountable, together with interest after such rate as the Court thinks just, or to contribute sums of money to the assets of the company by way of compensation in respect of such misapplication, retainer, misfeasance, or breach of trust as the Court thinks just.

(2) The provisions of this section shall apply in the winding-up of any company under the Companies Act, whether the same is being wound up

by or subject to the supervision of the Court, or is being wound up voluntarily, and whether the winding-up commenced before or after the passing of this Act, and notwithstanding that the offence is one for which the offender may be criminally responsible.

COMPANIES ACT, 1898.

61 and 62 Vict. c. 26.

1.—(1) Whenever, before or after the commencement of this Act, any shares in the capital of any company under the Companies Acts 1862 and 1890, credited as fully or partly paid up, shall have been or may be issued for a consideration other than cash, and at or before the issue of such shares no contract or no sufficient contract is filed with the Registrar of Joint Stock Companies, in compliance with section twenty-five* of the Companies Act 1867, the company or any person interested in such shares or any of them may apply to the Court for relief, and the Court, if satisfied that the omission to file a contract or sufficient contract was accidental or due to inadvertence, or that for any reason it is just and equitable to grant relief, may make an order for the filing with the Registrar of a sufficient contract in writing, and directing that on such contract being filed within a specified period it shall, in relation to such shares, operate as if it had been duly filed with the Registrar aforesaid before the issue of such shares.

(2) Any such application may be made in the manner in which an application to rectify the Register of Members may be made under section thirty-five of the Companies Act 1862, and either before or after an order has been made or an effective resolution has been passed for the winding-up of such company, and either before or after the commencement of any proceedings for enforcing the liability on such shares consequent on the omission aforesaid, and any such application shall, if not made by the company, be served on the company.

(3) Any such order may be made on such terms and conditions as the Court may think fit, and the Court may make such order as to costs as it deems proper, and may direct that an office copy of the order shall be filed with the Registrar aforesaid, and the order shall in all respects have full effect.

(4) Where the Court in any such case is satisfied that the filing of the requisite contract would cause delay or inconvenience, or is impracticable, it may, in lieu thereof, direct the filing of a memorandum in writing, in a

* After January 1st 1901 no proceedings are to be commenced under s. 25 of the Companies Act 1867, which is repealed by the Companies Act 1900, s. 33.

form approved by the Court, specifying the consideration for which the shares were issued, and may direct that on such memorandum being filed within a specified period it shall in relation to such shares operate as if it were a sufficient contract in writing within the meaning of section twenty-five of the Companies Act 1867, and had been duly filed with the Registrar aforesaid before the issue of such shares. The memorandum shall before the filing thereof be stamped with the same amount of *ad valorem* stamp duty as would be chargeable upon the requisite contract, unless the contract has been produced to the Registrar duly stamped, or unless the Registrar is otherwise satisfied that the contract was duly stamped.

2.—The jurisdiction by the Act given to the Court is not by implication to curtail or derogate from its jurisdiction to grant relief in any such case under section thirty-five of the Companies Act 1862, or otherwise.

COMPANIES ACT, 1900.

63 and 64 Vict. c. 48.

Allotment.

4.—(1) No allotment shall be made of any share capital of a company offered to the public for subscription, unless the following conditions have been complied with, namely—

(a) the amount (if any) fixed by the memorandum or articles of association and named in the prospectus as the minimum subscription upon which the directors may proceed to allotment; or

(b) if no amount is so fixed and named, then the whole amount of the share capital so offered for subscription,

has been subscribed, and the sum payable on application for the amount so fixed and named, or for the whole amount offered for subscription, has been paid to and received by the company.

(2) The amount so fixed and named and the whole amount aforesaid shall be reckoned exclusively of any amount payable otherwise than in cash, and is in this Act referred to as the minimum subscription.

(3) The amount payable on application on each share shall not be less than five per cent. of the nominal amount of the share.

(4) If the conditions aforesaid have not been complied with on the expiration of forty days after the first issue of the prospectus all money received from applicants for shares shall be forthwith repaid to the applicants without interest, and, if any such money is not so repaid within forty-eight days after the issue of the prospectus, the directors of the company shall be jointly and severally liable to repay that money

with interest at the rate of five per centum per annum from the expiration of the forty-eight days : Provided that a director shall not be liable if he proves that the loss of the money was not due to any misconduct or negligence on his part.

(5) Any condition requiring or binding any applicant for shares to waive compliance with any requirement of this section shall be void.

(6) This section, except subsection (3) thereof, shall not apply to any allotment of shares subsequent to the first allotment of shares offered to the public for subscription.

5.—(1) An allotment made by a company to an applicant in contravention of the foregoing provisions of this Act shall be voidable at the instance of the applicant within one month after the holding of the statutory meeting of the company and not later, and shall be so voidable, notwithstanding that the company is in course of being wound up.

(2) If any director of a company knowingly contravenes or permits or authorises the contravention of any of the foregoing provisions of this Act with respect to allotment he shall be liable to compensate the company and the allottee respectively for any loss, damages, or costs, which the company or the allottee may have sustained or incurred thereby : Provided that proceedings to recover such loss, damages, or costs shall not be commenced after the expiration of two years from the date of the allotment.

6.—(1) A company shall not commence any business or exercise any borrowing powers unless—

- (a) shares held subject to the payment of the whole amount thereof in cash have been allotted to an amount not less in the whole than the minimum subscription ; and
- (b) every director of the company has paid to the company on each of the shares taken or contracted to be taken by him, and for which he is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on the shares offered for public subscription ; and
- (c) there has been filed with the Registrar a statutory declaration by the secretary or one of the directors, in the prescribed form, that the aforesaid conditions have been complied with.

(2) The Registrar shall, on the filing of this statutory declaration, certify that the company is entitled to commence business, and that certificate shall be conclusive evidence that the company is so entitled.

(3) Any contract made by a company before the date at which it is entitled to commence business shall be provisional only, and shall not

be binding on the company until that date, and on that date it shall become binding.

(4) Nothing in this section shall prevent the simultaneous offer for subscription of any shares and debentures or the receipt of any application.

(5) If any company commences business or exercises borrowing powers in contravention of this section, every person who is responsible for the contravention shall, without prejudice to any other liability, be liable to a fine not exceeding fifty pounds for every day during which the contravention continues.

(6) Nothing in this section shall apply to a company registered before the commencement of this Act.

(7) This section shall not apply to any company where there is no invitation to the public to subscribe for its shares.

7.—(1) Whenever a company limited by shares makes any allotment of its shares the company shall within one month thereafter file with the Registrar—

- (a) a return of the allotments, stating the number and nominal amount of the shares comprised in the allotment, the names, addresses, and descriptions of the allottees, and the amount (if any) paid or due and payable on each share; and
- (b) in the case of shares allotted in whole or in part for a consideration other than cash, a contract in writing constituting the title of the allottee to such allotment, together with any contract of sale, or for services or other consideration in respect of which such allotment was made, such contracts being duly stamped, and a return stating the number and nominal amount of shares so allotted, the extent to which they are to be treated as paid up, and the consideration for which they have been allotted.

(2) If default is made in complying with the requirements of this section, every director, manager, secretary, or other officer of the company, who is knowingly a party to the default, shall be liable to a fine not exceeding fifty pounds for every day during which the default continues.

8.—(1) Upon any offer of shares to the public for subscription, it shall be lawful for a company to pay a commission to any person in consideration of his subscribing or agreeing to subscribe, whether absolutely or conditionally, for any shares in the company, or procuring or agreeing to procure subscriptions, whether absolute or conditional, for any shares in the company, if the payment of the commission and the amount or rate per cent. of the commission paid or agreed to be paid

are respectively authorised by the articles of association and disclosed in the prospectus, and the commission paid or agreed to be paid does not exceed the amount or rate so authorised.

(2) Save as aforesaid no company shall apply any of its shares or capital money, either directly or indirectly, in payment of any commission, discount, or allowance, to any person in consideration of his subscribing or agreeing to subscribe, whether absolutely or conditionally, for any shares of the company, or procuring or agreeing to procure subscriptions, whether absolute or conditional, for any shares in the company, whether the shares or money be so applied by being added to the purchase-money of any property acquired by the company or to the contract price of any work to be executed for the company, or the money be paid out of the nominal purchase-money or contract price, or otherwise.

(3) But nothing in this section shall affect the power of any company to pay such brokerage as it has heretofore been lawful for a company to pay.

Prospectus.

9.—(1) Every prospectus issued by or on behalf of a company or in relation to any intended company shall be dated, and that date shall, unless the contrary be proved, be taken as the date of publication of the prospectus.

(2) A copy of every such prospectus shall be signed by every person who is named therein as a director or proposed director of the company, or by his agent authorised in writing, and shall be filed with the Registrar on or before the date of its publication.

(3) The Registrar shall not register any prospectus unless it is so dated and signed. No prospectus shall be issued until so filed for registration, and every prospectus shall state on the face of it that it has been so filed.

10.—(1) Every prospectus issued by or on behalf of a company, or by or on behalf of any person who is or has been engaged or interested in the formation of the company, must state—

(a) the contents of the memorandum of association, with the names, descriptions, and addresses of the signatories, and the number of shares subscribed for by them respectively; and the number of founders' or management shares, if any, and the nature and extent of the interest of the holders in the property and profits of the company; and

(b) the number of shares, if any, fixed by the articles of association as the qualification of a director, and any provision in the articles of association as to the remuneration of the directors; and

- (c) the names, descriptions, and addresses of the directors or proposed directors ; and
- (d) the minimum subscription on which the directors may proceed to allotment, and the amount payable on application and allotment on each share ; and in the case of a second or subsequent offer of shares, the amount offered for subscription on each previous allotment, and the amount actually allotted ; and the amount, if any, paid on such shares ; and
- (e) the number and amount of shares and debentures issued, or agreed to be issued, as fully or partly paid up otherwise than in cash, and in the latter case the extent to which they are so paid up, and in either case the consideration for which such shares or debentures have been issued or are proposed or intended to be issued ; and
- (f) the names and addresses of the vendors of any property purchased or acquired by the company, or proposed so to be purchased or acquired, which is to be paid for wholly or partly out of the proceeds of the issue offered for subscription by the prospectus, or the purchase or acquisition of which has not been completed at the date of publication of the prospectus, and the amount payable in cash, shares, or debentures, to the vendor, and where there is more than one separate vendor, or the company is a sub-purchaser, the amount so payable to each vendor ; and
- (g) the amount (if any) paid or payable as purchase-money in cash, shares, or debentures, of any such property as aforesaid, specifying the amount payable for goodwill ; and
- (h) the amount (if any) paid or payable as commission for subscribing or agreeing to subscribe, or procuring or agreeing to procure subscriptions, for any shares in the company, or the rate of any such commission ; and
- (i) the amount or estimated amount of preliminary expenses ; and
- (j) the amount paid or intended to be paid to any promoter and the consideration for any such payment ; and
- (k) the dates of and parties to every material contract, and a reasonable time and place at which any material contract or a copy thereof may be inspected : Provided that this requirement shall not apply to a contract entered into in the ordinary course of the business carried on or intended to be carried on by the company, or to any contract entered into more than three years before the date of publication of the prospectus ; and
- (l) the names and addresses of the Auditors (if any) of the company ; and

(m) full particulars of the nature and extent of the interest (if any) of every director in the promotion of or in the property proposed to be acquired by the company, with a statement of all sums paid or agreed to be paid to him in cash or shares by any person either to qualify him as a director or otherwise for services rendered by him in connection with the formation of the company.

(2) For the purposes of this section every person shall be deemed to be a vendor who has entered into any contract, absolute or conditional, for the sale or purchase, or for any option of purchase, of any property to be acquired by the company, in any case where—

(a) the purchase-money is not fully paid at the date of publication of the prospectus; or

(b) the purchase-money is to be paid or satisfied wholly or in part out of the proceeds of the issue offered for subscription by the prospectus; or

(c) the contract depends for its validity or fulfilment on the result of such issue.

(3) Where any of the property to be acquired by the company is to be taken on lease this section shall apply as if the expression "vendor" included the lessor, and the expression "purchase-money" included the consideration for the lease, and the expression "sub-purchaser" included a sub-lessee.

(4) This section shall not apply to a circular or notice inviting existing members or debenture-holders of a company to subscribe for further shares or debentures, but subject as aforesaid, this section shall apply to any prospectus whether issued on or with reference to the formation of a company or subsequently: Provided that—

(a) the requirements as to the memorandum of association, and the qualification, remuneration, and interest of directors, the names, descriptions, and addresses of directors or proposed directors, and the amount or estimated amount of preliminary expenses, shall not apply in the case of a prospectus published more than one year after the date at which the company is entitled to commence business; and

(b) in the case of a prospectus published more than one year after the date at which the company is entitled to commence business, the obligation to disclose all material contracts shall be limited to a period of two years immediately preceding the publication of the prospectus.

(5) Any condition requiring or binding any applicant for shares or debentures to waive compliance with any requirement of this section, or

purporting to affect him with notice of any contract, document, or matter not specifically referred to in the prospectus, shall be void.

(6) Where any such prospectus as is mentioned in this section is published as a newspaper advertisement, it shall not be necessary to specify the contents of the memorandum of association or the signatories thereto, and the number of shares subscribed for by them.

(7) In the event of non-compliance with any of the requirements of this section, a director or other person responsible for the prospectus shall not incur any liability by reason of the non-compliance, if he proves that—

- (a) as regards any matter not disclosed, he was not cognisant thereof ;
or
- (b) the non-compliance arose from an honest mistake of fact on his part.

Provided that in the event of non-compliance with the requirements contained in paragraph (m) of sub-section (1) of this section no director or other person shall incur any liability in respect of such non-compliance unless it be proved that he had knowledge of the matters not disclosed.

(8) Nothing in this section shall limit or diminish any liability which any person may incur under the general law apart from this section.

11.—A company shall not prior to the statutory meeting vary the terms of a contract referred to in the prospectus, except subject to the approval of the statutory meeting.

Statutory Meeting.

12.—(1) Every company limited by shares and registered after the commencement of this Act shall, within a period of not less than one month or more than three months from the date at which the company is entitled to commence business, hold a general meeting of the members of the company, which shall be called the statutory meeting.

(2) The directors shall, at least seven days before the day on which the meeting is held, forward to every member of the company a report certified by not less than two directors of the company, or, where there are less than two directors, by the sole director and manager, stating—

- (a) the total number of shares allotted, distinguishing shares allotted as fully or partly paid up otherwise than in cash, and stating in the case of shares partly paid up the extent to which they are so paid up, and in either case the consideration for which they have been allotted ;
- (b) the total amount of cash received by the company in respect of such shares, distinguished as aforesaid ;

- (c) an abstract of the receipts and payments of the company on Capital Account to the date of the report, and an account or estimate of the preliminary expenses of the company ;
- (d) the names, addresses, and descriptions of the directors, Auditors (if any), manager (if any), and secretary of the company ; and
- (e) the particulars of any contract, the modification of which is to be submitted to the meeting for its approval, together with the particulars of the modification or proposed modification.

(3) The report shall, so far as it relates to the shares allotted by the company, and to the cash received in respect of such shares, and to the receipts and payments of the company on Capital Account, be certified as correct by the Auditors (if any) of the company.

(4) The directors shall cause a copy of the report, certified as by this section required, to be filed with the Registrar forthwith after the sending thereof to the members of the company.

(5) The directors shall cause a list showing the names, descriptions, and addresses of the members of the company, and the number of shares held by them respectively, to be produced at the commencement of the meeting, and to remain open and accessible to any member of the company during the continuance of the meeting.

(6) The members of the company present at the meeting shall be at liberty to discuss any matter relating to the formation of the company, or arising out of the report, whether previous notice has been given or not, but no resolution of which notice has not been given in accordance with the articles of association may be passed.

(7) The meeting may adjourn from time to time, and at any such adjourned meeting any resolution of which notice has been given in accordance with the articles of association, either before or subsequently to the former meeting, may be passed, and the adjourned meeting shall have the same powers as an original meeting.

(8) If default is made in filing such report as aforesaid or in holding the statutory meeting, then, at the expiration of fourteen days after the last day on which the meeting ought to have been held, any shareholder may petition the Court for the winding up of the company, and upon the hearing of the petition the Court may either direct that the company be wound up, or give directions for the report being filed or a meeting being held, or make any such order as may be just, and may order that the costs of the petition be paid by any persons who in the opinion of the Court are responsible for the default.

Mortgages and Charges.

14.—(1) Every mortgage or charge created by a company after the commencement of this Act and being either—

- (a) a mortgage or charge for the purpose of securing any issue of debentures; or
- (b) a mortgage or charge on uncalled capital of the company; or
- (c) a mortgage or charge created or evidenced by an instrument which, if executed by an individual, would require registration as a bill of sale; or
- (d) a floating charge on the undertaking or property of the company shall, so far as any security on the company's property or undertaking is thereby conferred, be void against the liquidator and any creditor of the company, unless filed with the Registrar for registration in manner required by this Act within twenty-one days after the date of its creation, but without prejudice to any contract or obligation for repayment of the money thereby secured.

(2) Where the mortgage or charge comprises property outside the United Kingdom it shall, so far as that property is concerned, be sufficient compliance with the requirements of this section, if a deed purporting to specifically charge such property be registered, notwithstanding that further proceedings may be necessary to make such mortgage or charge valid or effectual according to the law of the country in which such property is situate.

(3) The Registrar shall keep, with respect to each company, a register in the prescribed form of all such mortgages and charges created by the company after the commencement of this Act, and requiring registration under this section, and shall, on payment of the prescribed fee, enter in the register, with respect to every such mortgage or charge, the date of creation, the amount secured by it, short particulars of the property mortgaged or charged, and the names of the mortgagees, or persons entitled to the charge.

(4) Provided that where a series of debentures containing any charge to the benefit of which the debenture-holders of that series are entitled *pari passu* is created by a company, it shall be sufficient to enter on the register—

- (a) the total amount secured by the whole series; and
- (b) the dates of the resolutions creating the series and of the covering deed, if any, by which the security is created or defined; and
- (c) a general description of the property charged; and
- (d) the names of the trustees, if any, for the debenture-holders.

(5) Where more than one issue is made of debentures in the same series, the company may require the Registrar to enter on the register the date and amount of any particular issue, but an omission to do this shall not affect the validity of the debentures issued.

(6) The Registrar shall give a certificate under his hand of the registration of any mortgage or charge registered in pursuance of this section, stating the amount thereby secured (which certificate shall be conclusive evidence that the requirements of this section as to registration have been complied with), and the company shall cause a copy of the certificate so given to be endorsed on every debenture or certificate of debenture stock which is issued by the company, and the payment of which is secured by the mortgage or charge so registered.

(7) It shall be the duty of the company to register every mortgage or charge created by the company and requiring registration under this section, and for that purpose to supply the Registrar with the particulars required for registration; but any such mortgage or charge may be registered on the application of any person interested therein.

(8) The register kept, in pursuance of this section, of the mortgages and charges of each company shall be open to inspection by any person on payment of the prescribed fee, not exceeding one shilling for each inspection.

(9) Every company shall cause a copy of every instrument creating any mortgage or charge requiring registration under this section to be kept at the registered office of the company, and to be open to inspection by the members and creditors of the company on payment of such fee, not exceeding one shilling for each inspection, as may be fixed by the regulations of the company. Provided that in the case of a series of uniform debentures a copy of one such debenture shall be sufficient.

15.—A Judge of the High Court, on being satisfied that the omission to register a mortgage or charge within the time required by this Act, or the omission or misstatement of any particular with respect to any such mortgage or charge, was accidental, or due to inadvertence or to some other sufficient cause, or is not of a nature to prejudice the position of creditors or shareholders of the company, or that on other grounds it is just and equitable to grant relief, may, on the application of the company or any person interested, and on such terms and conditions as seem to the Judge just and expedient, order that the time for registration be extended, or, as the case may be, that the omission or misstatement be rectified.

16.—The Registrar may, on evidence being given to his satisfaction that the debt for which any registered mortgage or charge was given has been paid or satisfied, order that a memorandum of satisfaction be

entered on the register, and shall if required furnish the company with a copy thereof.

17.—The Registrar shall keep a chronological index, in the prescribed form and with the prescribed particulars, to the mortgages or charges registered under this Act.

18.—If any company makes default in complying with the requirements of this Act as to the registration of any mortgage, or charge created by the company, the company and every director, manager, and other officer of the company, who knowingly and wilfully authorised or permitted such default shall, without prejudice to any other liability, be liable on summary conviction to a fine not exceeding one hundred pounds; and if any person knowingly and wilfully authorises or permits the delivery of any debenture or certificate of debenture stock required by this Act to be registered, without a copy of the certificate of the Registrar being endorsed upon it, he shall, without prejudice to any other liability, be liable on summary conviction to a fine not exceeding one hundred pounds.

Annual Summary.

19.—(1) The summary mentioned in section twenty-six of the Companies Act 1862 shall be so framed as to distinguish between the shares issued for cash and the shares issued otherwise than for cash or only partly for cash, and shall, in addition to the particulars required by that section to be specified, also specify—

- (a) the total amount of debt due from the company in respect of all mortgages and charges which require registration under this Act, or which would require such registration if created after the commencement of this Act; and
- (b) the names and addresses of the persons who are the directors of the company at the date of the summary.

(2) The list and summary mentioned in the said section twenty-six must be signed by the manager or by the secretary of the company.

20.—Sections forty-five and forty-six of the Companies Act 1862 shall apply to companies having a capital divided into shares, and the words "and not having a capital divided into shares" in those sections shall be repealed.

Audit.

21.—(1) Every company shall at each annual general meeting appoint an Auditor or Auditors to hold office until the next annual general meeting.

(2) If an appointment of Auditors is not made at an annual general meeting, the Board of Trade may, on the application of any member of the company, appoint an Auditor of the company for the current year, and fix the remuneration to be paid to him by the company for his services.

(3) A director or officer of the company shall not be capable of being appointed Auditor of the company.

(4) The first Auditors of the company may be appointed by the directors before the statutory meeting, and if so appointed shall hold office until the first annual general meeting, unless previously removed by a resolution of the shareholders in general meeting, in which case the shareholders at such meeting may appoint Auditors.

(5) The directors of a company may fill any casual vacancy in the office of Auditor, but while any such vacancy continues the surviving or continuing Auditor or Auditors, if any, may act.

22.—The remuneration of the Auditors of a company shall be fixed by the company in general meeting, except that the remuneration of any Auditors appointed before the statutory meeting, or to fill any casual vacancy, may be fixed by the directors.

23.—Every Auditor of a company shall have a right of access at all times to the books and accounts and vouchers of the company, and shall be entitled to require from the directors and officers of the company such information and explanation as may be necessary for the performance of the duties of the Auditors, and the Auditors shall sign a certificate at the foot of the Balance Sheet stating whether or not all their requirements as Auditors have been complied with, and shall make a report to the shareholders on the accounts examined by them, and on every Balance Sheet laid before the company in general meeting during their tenure of office; and in every such report shall state whether, in their opinion, the Balance Sheet referred to in the report is properly drawn up, so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company; and such report shall be read before the company in general meeting.

False Statements.

28.—If any person in any return, report, certificate, Balance Sheet, or other document, required by or for the purposes of this Act, wilfully makes a statement false in any material particular, knowing it to be false, he shall be guilty of a misdemeanour, and shall be liable on conviction on indictment to imprisonment for a term not exceeding two years, with or without hard labour, and on summary conviction to imprisonment for a term not exceeding four months, with or without

hard labour, and in either case to a fine in lieu of or in addition to such imprisonment as aforesaid: Provided that the fine imposed on summary conviction shall not exceed one hundred pounds.

Supplemental.

31.—This Act shall, except as otherwise expressed, apply to every company, whether formed before or after the commencement of this Act.

32.—The Companies (Winding-up) Act 1890, and this Act, shall have effect as part of the Companies Act 1862; but nothing in this section shall be construed as extending the Companies (Winding-up) Act 1890 to Scotland or Ireland.

33.—(1) Section twenty-five of the Companies Act 1867, and the other enactments mentioned in the schedule to this Act, to the extent specified in the third column of that schedule, are hereby repealed.

(2) No proceedings under section twenty-five of the Companies Act 1867 shall be commenced after the commencement of this Act.

34.—This Act shall apply to Scotland, subject to the following provisions and modifications:—

- (1) "Solicitor of the High Court" shall mean enrolled law agent;
- (2) The provisions of this Act with respect to the registration of mortgages and charges shall not apply to companies registered in Scotland;
- (3) All prosecutions for offences or fines shall be at the instance of the Lord Advocate or a procurator fiscal as the Lord Advocate may direct.

35.—This Act shall, except as otherwise expressed, come into operation on the first day of January one thousand nine hundred and one.

36.—This Act may be cited as the Companies Act 1900, and may be cited with the Companies Acts 1862 to 1898.

SCHEDULE.

ENACTMENTS REPEALED.

Session and Chapter	Short Title	Extent of Repeal
25 & 26 Vict. c. 89	The Companies Act, 1862	Section eighteen, from "A certificate" to the end of the section In sections forty-five and forty-six, the words "and not having a capital divided into shares"
30 & 31 Vict. c. 131	The Companies Act, 1867	Section one hundred and ninety-two Sections twenty-five, thirty-eight, and thirty-nine

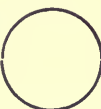
No. of Certificate .

FORM No. 6A.

THE COMPANIES ACTS, 1862 TO 1900.

FORM E.

as altered by the Board of Trade,
by Notices in the *London Gazette*,
pursuant to s. 71 of the Com-
panies Act, 1862, and s. 19 of
the Companies Act, 1900.



A 5s. Companies' Registration Fee
Stamp must be impressed here.

Summary of Capital and Shares.

of the.....

.....
Company, Limited, made up to the.....day of.....190....
(being the fourteenth day succeeding the date of the First Ordinary
General Meeting in the year).

Nominal Capital, £....Divided into*.....Shares of £.....* each.

Total Number of Shares taken up to the.....day of..... {
190....(which number must agree with the total shown in {
the list, as held by existing members).*

Number to be paid for wholly in cash

Number issued as partly paid up to the extent of.....per
share otherwise than for cash

Number issued as fully paid up otherwise than for cash.. ..

‡ There has been called up on each of.....Shares £

" " " " £

" " " " £

§ Total amount of Calls received, including payments on appli-
cation and allotment £

Total amount (if any) agreed to be considered as paid on.....

Shares which have been issued as fully paid (otherwise than in
cash) £

Total amount (if any) agreed to be considered as paid on.....

Shares which have been issued as partly paid up to the
extent of.....per Share £

Total amount of *Calls* unpaid £

* Where there are Shares of different kinds or amounts (e.g., Preference and Ordinary, or £10 and £5) state the numbers and nominal value separately.

‡ Where various amounts have been called, or there are Shares of different kinds state them separately.

§ Include what has been received on forfeited, as well as on existing, Shares.

Total amount (if any) paid on ||Shares forfeited £
 Total amount of debt due from the Company in respect of mort-
 gages and charges which require registration under the Com-
 panies Act, 1900, at the date to which this Summary is made
 up £

NOTE.—A list of the names and addresses of the Directors must follow the list of Members. Banking Companies must also add a list of all their places of business.

The return must be signed, *at the end*, by the Manager or Secretary of the Company.

Presented for filing by

LIST of Persons holding Shares in the _____ Company,
 Limited, on the _____ day of _____ 190 _____, and of Persons
 who have held shares therein at any time since the date of the
 last Return, showing their Names and Addresses, and an Account
 of the Shares so held [*entered under the following headings*] :—

Folio in Register Ledger, containing particulars.

Names, Addresses, and Occupations—

Surname,

Christian Name,

Address,

Occupation.

Account of Shares—

* Number of Shares held by existing Members at date of Return.†

† Particulars of Shares Transferred since the date of the last Return
 by persons who are still Members :

Number,†

Date of Registration of Transfer.

† Particulars of Shares Transferred since the date of the last Return
 by persons who have ceased to be Members :

Number,†

Date of Registration of Transfer.

Remarks.

(Signature)

(Officer)

* The aggregate Number of Shares held, and not the Distinctive Numbers, is to be stated, and the column must be added up throughout, so as to make one total to agree with that stated in the Summary to have been taken up.

† When the Shares are of different classes these columns may be subdivided so that the number of each class held, or transferred, may be shown separately.

† The date of Registration of each Transfer should be given as well as the Number of Shares transferred on each date. The particulars should be placed opposite the name of the Transferor, and not opposite that of the Transferee, but the name of the Transferee may be inserted in the "Remarks" column, immediately opposite the particulars of each Transfer.

|| State the aggregate number of Shares forfeited (if any).

No. of Certificate .

FORM No. 6B.

Names and Addresses of the persons who are the Directors of the
 , Lim., on the day of 190 .

(Pursuant to s. 19 (1) (b) of 63 and 64 Vict. c. 48.)

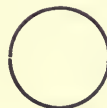
Names	Addresses
	Signature Description (i.e., Manager or Secretary.)

Note.—This List should be annexed to the Annual Return immediately after the List of Members.

No. of Certificate .

FORM No. 9.

THE COMPANIES ACTS, 1862 TO 1900.



A 5s. Companies'
 Registration Fee
 Stamp must
 be impressed here.

Copy of Register of Directors or Managers of the
 Company, . Pursuant to Sections 45 and 46 of 25 and 26
 Vict. c. 89, and Section 20 of 63 and 64 Vict. c. 48.

This Notice should be signed by the Secretary of the Company.

Presented for filing by

Copy of the Register of Directors or Managers of the
 Company, , and of any changes therein.

Names	Addresses	Occupations	* Changes
			(Signature)

* A complete list of the existing Directors or Managers should always be given. A note of the changes since the last list was filed should be made in this column, e.g., by placing against a new Director's name the words "in place of" and by writing against any former Director's name the words "dead," "resigned," or as the case may be.

member of the company; and to be filed with the Registrar forthwith after the sending thereof to the members of the company (Section 12 (4)).

NOTE.—This form has been provided for the purpose of indicating the nature of the information that is required; but as the report to be filed must be a copy of that sent to the shareholders, all that is contained in that report must appear in this.

(a) The total number of shares allotted is _____ of which are _____ allotted (1) _____ in consideration of _____ and upon each of the remaining shares the sum of _____ has been paid in cash.

(b) The total amount of cash received by the company in respect of the shares issued wholly for cash is £ _____, and on the shares issued partly for cash is £ _____.

(c) The receipts and payments of the company on Capital Account to the date of this report are as follows:

Particulars of Receipts				Particulars of Payments			

Presented for filing by _____.

The following is an account (or estimate) of the preliminary expenses of the company.

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(d) Names, addresses, and descriptions of the Directors, Auditors (if any), Manager (if any), and Secretary of the company.

DIRECTORS.

Surname	Christian Name	Address	Description

(1) Here state as "fully paid up" or "paid up otherwise than in cash to the extent of _____ per share."

AUDITORS.

Surname	Christian Name	Address	Description

MANAGER.

--	--	--	--

SECRETARY.

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(e) Particulars of any contract the modification of which is to be submitted to the meeting for its approval, together with the particulars of the modification or proposed modification.

We hereby certify this Report,

} Two
Directors.

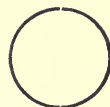
We hereby certify that so much of this Report as relates to the Shares allotted by the company and to the Cash received in respect of such Shares and to the receipts and payments of the company on Capital Account is correct.

} Auditors.

No. of Certificate

FORM No. 47.

THE COMPANIES ACTS, 1862 TO 1900.



PARTICULARS to be supplied to the Registrar pursuant to Section 14 (7) of the Companies Act, 1900 (63 and 64 Vict. c. 48), of a Mortgage or Charge created by the _____ Lim., and being:—

- * (a) A mortgage or charge for the purpose of securing any issue of debentures; or

* Strike out the Sub-heads (a), (b), (c), or (d), which do not apply.

- (b) a mortgage or charge on uncalled capital of the company ; or
- (c) a mortgage or charge created or evidenced by an instrument, which, if executed by an individual, would require registration as a bill of sale ; or
- (d) a floating charge on the undertaking or property of the company.

(NOTE.—The original instrument evidencing the mortgage or charge must be presented with this return within twenty-one days after the date of its creation (Section 14 (1)), accompanied by the particulars set out on this form.)

Presented for filing by

Particulars of a Mortgage or Charge created by the Lim.,

[entered under the following headings]:—

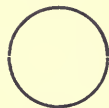
- (1) Date of creation of the Mortgage or Charge ; or, in the case of a series of Debentures, the date of the Covering Deed (if any) by which the Security is created or defined.
- (2) Amount secured by the Mortgage or Charge ; or, in the case of a series of Debentures, the total amount secured by the whole series.
- (3) Dates of Resolutions creating the series of Debentures.
- (4) Short Particulars of the Property Mortgaged or Charged ; or, in the case of a series of Debentures, a *General* Description of the Property Charged.
- (5) Names (with Addresses and Descriptions) of the Mortgagees or Persons entitled to the charge ; or, in the case of a series of Debentures, the names, &c., of the Trustees (if any), for the Debenture-holders.
- (6) Where more than one issue of Debentures in same series—
 Date of present issue :
 Amount of present issue :
 Total amount previously issued of this series (if any)

(Signature)

Certificate No. .

FORM No. 49.

THE COMPANIES ACTS, 1862 TO 1900.



Memorandum of satisfaction of Mortgage or Charge created by the _____, Lim., to be entered on the register pursuant to Section 16 of the Companies Act, 1900 (63 & 64 Vict. c. 48).

Presented for filing by _____.

To the Registrar of Joint Stock Companies.

The _____, Lim., hereby gives notice that the (a) _____, dated the _____ day of _____ one thousand nine hundred and _____, and created by the company for securing the sum of £ _____ was satisfied to the extent of £ _____ on the _____ day of _____ 190 _____.

In witness whereof the common seal of the company was hereunto
affixed the day of one thousand nine hundred and
 in the presence of

} Directors.

L. S.

Secretary. '

PARLIAMENTARY COMPANIES.

THE COMPANIES CLAUSES CONSOLIDATION
ACT, 1845.

8 Vict. c. 16.

Register of Shareholders.

9.—The company shall keep a book to be called the "Register of Shareholders," and in such book shall be fairly and distinctly entered, from time to time, the names of the several corporations, and the names and addresses of the several persons entitled to shares in the company, together with the number of shares to which such shareholders shall be respectively entitled, distinguishing each share by its

(a) Insert here "Mortgage" or "Charge" "Debentures" or "Debenture-Stock" as the case may be.

number and the amount of the subscriptions paid on such shares, and the surnames or corporate names of the said shareholders shall be placed in alphabetical order; and such book shall be authenticated by the common seal of the company being affixed thereto; and such authentication shall take place at the first ordinary meeting, or at the next subsequent meeting of the company, and so from time to time at each ordinary meeting of the company.

Addresses of Shareholders.

10.—In addition to the said Register of Shareholders, the company shall provide a book to be called the "Shareholders' Address Book," in which the secretary shall, from time to time, enter in alphabetical order the corporate names and places of business of the several shareholders of the company, being corporations, and the surnames of the several other shareholders, with their respective Christian names, places of abode, and descriptions, so far as the same shall be known to the company.

Register of Mortgages and Bonds.

45.—A register of mortgages and bonds shall be kept by the secretary, and within fourteen days after the date of any such mortgage or bond an entry or memorial, specifying the number and date of such mortgage or bond and the sums secured thereby, and the names of the parties thereto, with their proper additions, shall be made in such register.

Register of Stock.

63.—The company shall, from time to time, cause the names of the several parties who may be interested in any such stock as aforesaid, with the amount of the interest therein possessed by them respectively, to be entered in a book to be kept for the purpose, and to be called "The Register of Holders of Consolidated Stock."

Election of Auditors.

101.—Except where, by the special Act, Auditors shall be directed to be appointed otherwise than by the company, the company shall, at the first ordinary meeting after the passing of the special Act, elect the prescribed number of Auditors, and, if no number is prescribed, two Auditors, in like manner as is provided for the election of directors; and at the first ordinary meeting of the company in each year thereafter the company shall in like manner elect an Auditor to supply the place of the Auditor then retiring from office, according to

the provision hereinafter contained; and every Auditor elected as hereinbefore provided, being neither removed nor disqualified nor having resigned, shall continue to be an Auditor until another be elected in his stead.

102.—Where no other qualification shall be prescribed by the special Act, every Auditor shall have at least one share in the undertaking; and he shall not hold any office in the company, nor be in any other manner interested in its concerns except as a shareholder.

103.—One of such Auditors (to be determined in the first instance by ballot between themselves, unless they shall otherwise agree, and afterwards by seniority) shall go out of office at the first ordinary meeting in each year; but the Auditor so going out shall be immediately re-eligible, and after any such re-election shall, with respect to the going out of office by rotation, be deemed a new Auditor.

104.—If any vacancy take place among the Auditors in the course of the current year, then, at any general meeting of the company, the vacancy may, if the company think fit, be supplied by election of the shareholders.

105.—The provision of this Act respecting the failure of an ordinary meeting at which directors ought to be chosen shall apply, *mutatis mutandis*, to any ordinary meeting at which an Auditor ought to be appointed.

Powers and Duties of Auditors.

106.—The directors shall deliver to such Auditors the half-yearly or other periodical accounts and Balance Sheet fourteen days at the least before the ensuing ordinary meeting at which the same are required to be produced to the shareholders, as hereinafter provided.

107.—It shall be the duty of such Auditors to receive from the directors the half-yearly or other periodical accounts and Balance Sheet required to be presented to the shareholders, and to examine the same.

108.—It shall be lawful for the Auditors to employ such accountants and other persons as they may think proper, at the expense of the company, and they shall either make a special report on the said accounts or simply confirm the same; and such report or confirmation shall be read, together with the report of the directors, at the ordinary meeting.

Accounts.

115.—The Directors shall cause full and true accounts to be kept of all sums of money received or expended on account of the company by the directors and all persons employed by or under them, and of the matters and things for which such sums of money shall have been received or disbursed and paid.

116.—The books of the company shall be balanced at the prescribed periods, and, if no periods be prescribed, fourteen days at least before each ordinary meeting; and, forthwith, on the books being so balanced, an exact Balance Sheet shall be made up, which shall exhibit a true statement of the capital, stock, credits, and property of every description belonging to the company, and the debts due by the company at the date of making such Balance Sheet, and a distinct view of the profit or loss which shall have arisen on the transactions of the company in the course of the preceding half year; and previously to each ordinary meeting such Balance Sheet shall be examined by the directors, or any three of their number, and shall be signed by the chairman or deputy-chairman of the directors.

118.—The directors shall produce to the shareholders assembled at such ordinary meeting the said Balance Sheet, applicable to the period immediately preceding such meeting, together with the report of the Auditors thereon, as hereinbefore provided.

Dividends.

120.—Previously to every ordinary meeting at which a dividend is intended to be declared, the directors shall cause a scheme to be prepared showing the profits (if any) of the company for the period current since the preceding ordinary meeting at which a dividend was declared, and apportioning the same, or so much thereof as they may consider applicable to the purposes of dividend, among the shareholders, according to the shares held by them respectively, the amount paid thereon, and the periods during which the same may have been paid, and shall exhibit such scheme at such ordinary meeting, and at such meeting a dividend may be declared according to such scheme.

121.—The company shall not make any dividend whereby their capital stock will be in any degree reduced: provided always that the word "dividend" shall not be construed to apply to a return of any portion of the capital stock, with the consent of all the mortgagees and bond creditors of the company, due notice being given for that purpose at an extraordinary meeting to be convened for that object.

122.—Before apportioning the profits to be divided among the shareholders the directors may, if they think fit, set aside thereout such sum as they may think proper to meet contingencies, or for enlarging, repairing, or improving the works connected with the undertaking, or any part thereof, and may divide the balance only among the shareholders.

123.—No dividend shall be paid in respect of any share, until all calls then due in respect of that and every other share held by the person to whom such dividend may be payable shall have been paid.

THE COMPANIES' CLAUSES ACT, 1863.

26 and 27 Vict. c. 118.

Issues of Preference Shares and Stock.

13.—Where any such company is authorised by any special Act hereafter passed and incorporating this part of this Act to raise any additional sum or sums by the issue of new preference shares, or by the issue of new preference stock, or (at the option of the company) by either of those modes, then and in every such case the company, with the like sanction as aforesaid, may for the purpose of raising such additional sum or sums from time to time create and issue (according as the authority given by the special Act extends to shares only or to stock only or to both) such new shares or new stock either ordinary or preference, and either of one class and with like privileges, or of several classes and with different privileges, and of the same or different amounts, and respectively with any fixed, fluctuating, contingent, preferential, perpetual, terminable, deferred, or other dividend or interest, not exceeding the rate prescribed in the special Act; and if no rate is prescribed, then not exceeding the rate of five pounds per centum per annum, and subject (as to any such new shares) to the payment of calls of such amounts and at such times as the company from time to time thinks fit.

Provided always that any preference assigned to any shares or stock so issued under the special Act shall not affect any guarantee or any preference or priority in the payment of dividend or interest, on any shares or stock that may have been granted by the company under or confirmed by any previous Act, or that may be otherwise lawfully subsisting.

Preference Dividends not Cumulative.

14.—The preference shares or preference stock shall be entitled to the preferential dividend, or interest assigned thereto, out of the profits of each year in priority to the ordinary shares and ordinary stock of the company; but if in any year ending on the day prescribed in the special Act, and if no day is prescribed, then on the thirty-first day of December, there are not profits available for the payment of the full amount of preferential dividend or interest for that year, no part of the deficiency shall be made good out of the profits of any subsequent year, or out of any other funds of the company.

Separate Accounts of Debenture Stock.

33.—Separate and distinct accounts shall be kept by the company showing how much money has been received for or on account of debenture stock, and how much money borrowed or owing on mortgage or bond, or which they have power so to borrow, has been paid off by debenture stock, or raised thereby, instead of being borrowed on mortgage or bond.

THE COMPANIES CLAUSES ACT, 1869.

32 and 33 Vict. c. 48.

Power to Issue Shares or Stock at a Discount.

5.—Section 21 of the Companies Clauses Act 1863 shall, with respect to any company to which it is applicable under the provisions of this or any other Act, be read and have effect as if the following words—that is to say, "but so that not less than the full nominal amount of any share or portion of stock be payable or paid in respect thereof," had not been inserted in that section.

6.—Any shares forming part of the capital (whether original or additional) authorised to be raised by any special Act of the company passed before the present Session which have not been disposed of may be disposed of in manner provided by Part II. of the Companies Clauses Act 1863, as amended by this Act, and that part, as so amended, shall be deemed incorporated with such special Act accordingly.

7.—Provided that any shares, the creation whereof has been authorised by the company, but which have not been issued before the passing of this Act, shall not be issued on any terms other than those whereon the same might have been issued if this Act had not been passed, unless and until the issue thereof on terms other than as aforesaid is after the passing of this Act authorised by the company in manner provided by Part II. of the Companies Clauses Act 1863.

8.—Provided always that this Act shall not be construed to alter or extend the provisions of any Act relating to share capital in respect of which the amount of profits to be divided is limited to a fixed rate per centum upon the paid-up capital of the company.

MINING COMPANIES.

THE STANNARIES ACT, 1869.

32 and 33 Vict. c. 19.

Interpretation.

2.—In this Act—

The term "Stannaries" means the Stannaries of Devon and Cornwall:

The term "company" includes any persons or partnership body working a mine in the Stannaries:

The term "purser" means the purser for the time being of a company, and if there is no purser, then the secretary for the time being, or if there is no secretary, then the principal agent for the time being of a company:

The term "Cost Book" includes all books and papers relating to the business of a mine, which are for the time being kept by a purser or which according to the custom of the Stannaries, or the directions of the Company, ought to be kept by him.

3.—This Act extends only to mines within the Stannaries, and subject to the jurisdiction of the Court, or within the cognisance of the Vice-Warden, and nothing in this Act shall extend to companies registered under any of the Joint Stock Companies Acts, except where such companies are expressly mentioned or necessarily implied.

Entry of Accounts.

9.—The purser of every company shall once at least in every four months truly enter in the Cost Book of the company accounts showing the actual financial position of the company at the end of the financial month of the company last preceding the time of entry, including a statement of all credits, debts, and liabilities, and distinguishing in such accounts the amount of calls paid and calls not paid, with accurate lists of all the shareholders for the time being in the company, with their respective addresses, corrected from time to time as occasion requires, and all other accounts, documents, and things which the purser is for the time being required to enter therein by the custom of the Stannaries, or by the directions of the company; and after the passing of this Act all existing or future companies having any rules or regulations touching the management of the company or conduct of the business of any mine shall file a true copy of them at the office of the Registrar without payment of any fee; and such rules or regulations shall be subject to the inspection of all applicants at reasonable times; and if any company shall neglect to file such rules or regulations as above required, then any shareholder in or creditor of any such company may apply for an order of the Court to file such rules or regulations forthwith, which order shall be enforced by the process of the Court.

Audit.

10.—At any meeting of the company, with special notice, the accounts of the company may be audited, and a call may be made.

THE STANNARIES ACT, 1887.

50 and 51 Vict. c. 43.

Interpretation.

2.—In this Act—

The term "company" means any persons or partnership body, joint stock company, company constituted under the Companies Act 1862, or any statutory modification thereof, and whether corporate or unincorporate, and whether limited or unlimited, engaged in or formed for working mines within the Stannaries:

The term "purser" means the purser for the time being of a company, or if there is no purser, then the secretary for the time being, or if there is no secretary, then the principal agent or manager for the time being of a company :

The term "Cost Book" includes all books and papers relating to the business of a mine which are for the time being kept by a purser, or which, according to law or the custom of the Stannaries, ought to be kept by him :

The term "lessors" means the lessor or grantor of any lease, or grant of any mine, or licence to exercise mining rights and powers, and includes every person entitled under any such lease, grant, or licence, or any other instrument whatever, to receive the rents or dues payable in respect of any mine :

The term "mortgagees" includes all holders of mortgage-debentures, mortgages, or other charges issued by any company :

The term "sheriff" includes any officer charged with the execution of a writ or other process :

The term "miners" includes all artisans, labourers, and other persons working in and about a mine, except the purser, secretary, agent, or manager :

The term "wages" includes all earnings by miners arising from any description of piece or other work, or as tributers or otherwise :

The term "mining effects" includes machinery, materials, goods, and chattels, and all ores and halvans, and all other personal property appertaining to a mine, or used or intended to be used for mining purposes.

Extent of Act.

3.—This Act extends only to metalliferous mines and tin streaming works within the Stannaries.

Mine Club Fines to be Accounted for.

13.—(1) After the commencement of this Act, any custom or rule of law to the contrary notwithstanding, all moneys deducted in any mine from the wages or earnings of or otherwise contributed by the miners for the purposes of a mine club, or accident, or sick or benefit fund, shall, unless a majority of the miners shall by resolution decide otherwise, be deemed to belong to the miners and not to the company, and the said moneys, and any contributions added thereto by the shareholders, shall be placed to a separate account, and the details thereof, showing the amount received and the several payments thereout, and

to whom made during each preceding sixteen weeks, shall be set out in the Balance Sheet to be presented to the shareholders at each ordinary meeting; and a copy of the same shall be posted in the miners' dry or changing sheds, and in the account house; and it shall be lawful for the miners in any mine, if they so please, to appoint any two of themselves to audit the said mine club fund accounts: Provided that section thirty-four of this Act shall not restrain the right of the miners to pass any such resolution, and such resolution shall have effect for twelve calendar months only after the passing thereof. And in the event of any money being so deducted for the purpose of medical attendance, each miner shall be entitled to name a qualified medical practitioner to whom the amount so deducted from his wages shall be paid for such medical attendance.

Power to pay over Club Funds to Registered Friendly Society.

14.—When deductions are made from the wages of miners for the maintenance of a mine club fund, under the provisions of the last preceding section of this Act, it shall be lawful for the miners employed in or about the mine by resolution of a majority of such miners to appoint a committee of management of such fund: Provided that if any portion of the said fund is contributed by the company, the sanction and concurrence of the said company shall be required in respect of the appointment of such committee; and such committee may transfer the same to any registered friendly society established for the whole or any part of the Stannaries district, and willing to receive the same upon such terms as may be agreed upon between the said committee and the said society.

Mortgages of Mining Plant and Effects to be Registered.

19.—All mortgages, mortgage debentures, and other documents whatever, whereby power is given by any company to any persons to take possession of any mining effects of or on a mine, shall, in addition to any registration thereof now required by law, be registered within twenty-eight days from the date thereof, at the office of the said Registrar, in a book to be kept there for that purpose, without payment of any fee, and such book shall be subject to the inspection of all applicants at all reasonable times, and no such mortgage, mortgage debenture, or other document, unless so registered, shall confer any priority over or title as against the claims of any persons whatever for work and labour done or services performed in or upon such mine, or for goods or materials supplied to any company by which the said mine is carried on; such registration shall not affect any priority in respect of wages under the provisions of this Act.

Accounts to be entered in Cost Book.

23.—The purser of every Cost Book mine shall, once at least every sixteen weeks, truly enter in the Cost Book of the mine accounts showing the actual financial position of the company at the end either of the financial month of such company last preceding the time of entry, or of the calendar month last preceding that time, including a statement of all credits, debts, and liabilities, and distinguishing in such accounts the amounts of calls paid, and calls not paid, and also all other accounts, documents, and things that the purser is required to enter therein by the custom of the Stannaries, or by the direction of the company, and if any purser shall fail to make such entries or any of them within the time or in manner above directed, he shall, when and so often as he shall so fail, be liable to a penalty not exceeding twenty pounds, to be recovered in a summary manner before any two or more justices of the peace.

Penalty for False Entries, &c.

24.—If in the said accounts any false statement or entry shall be made, or any material particular omitted with the knowledge of the purser, the said purser shall be liable in respect of every such false statement, entry, or omission to a penalty not exceeding fifty pounds, to be recovered in a summary manner before any two or more justices of the peace, and the said justices may, in their absolute discretion, award any portion of the penalty imposed by them (not exceeding one moiety thereof) to the prosecutor, provided he is a shareholder in the company or a person having a legal right to inspect the said accounts; if such false statement, entry, or material particular has been made or omitted with the knowledge of the manager of the mine, such manager shall also be liable to a like penalty, to be recovered in like manner and with the like discretion in the justices as to their apportionment thereof.

Meetings to be held Once every Sixteen Weeks.

25.—The purser of every Cost Book mine shall duly convene an ordinary meeting of the shareholders in such mine at least once every sixteen weeks, for the transaction of the ordinary business of the said mine, and at every such meeting the Cost Book of the said mine, containing the accounts and other matters required by this Act to be entered therein, together with a list showing the name and address of every shareholder from whom any call is in arrear and unpaid, and the amount of the calls unpaid by him, shall be laid before the meeting, and be open to full and unrestricted inspection by any shareholder

present, and if any purser shall fail to convene such meeting, or to duly hold the same, or shall fail to produce the said Cost Book thereat, or to permit it to be inspected as aforesaid, he shall forfeit for each and every such default a sum not exceeding ten pounds, to be recovered in a summary manner on the complaint of any shareholder in the company, before any two or more justices of the peace.

Accounts to be Printed.

26.—The accounts by the twenty-third section of this Act directed to be entered in the Cost Book shall, after the same have been laid before a meeting of the shareholders in pursuance of the twenty-fifth section, be printed, and a copy thereof sent to each shareholder in the company and also to the lessors of the mine.

Evasions of this Act to be Void.

34.—Any contract expressed or implied with the employers, or terms of hiring, which would in effect deprive miners of any right secured to them by this Act, or impose any condition whatever in reference to the disposition of club or benefit funds, shall, so far as such rights are affected, and in respect of any such condition, be void and of no effect.

Printed Copies of this Act to be Posted Up.

35.—Printed copies of this Act and of the rules and regulations for the time being in force in any mine, shall be kept posted up in the smiths' shop and in the miners' dry or changing shed of every mine.

THE STANNARIES COURT (ABOLITION)
ACT, 1896.

59 and 60 Vict. c. 45.

An Act for abolishing the Court of the Vice-Warden of the Stannaries.

1.—(1) On the commencement of this Act, the Court of the Vice-Warden of the Stannaries shall cease to exist except for the purpose of continuing and concluding proceedings pending in that Court at that date, and as from that date all jurisdiction and powers of the said Court and its officers shall, except as aforesaid, be transferred to and vested in such of the County Courts as the Lord Chancellor may by

order direct, and be exercised subject to and in accordance with rules of Court for regulating the procedure in County Courts.

(2) Provision may be made by order of the Lord Chancellor :—

(a) for determining by, to, or before what officer, or in what office, may be done anything required to be done by, to, or before any officer or in any office of the said Court of the Vice-Warden ;

(b) for transferring to a County Court any proceedings pending in the said Court at the commencement of this Act ;

(c) for determining the place of sitting for the exercise of any jurisdiction transferred by this Act ;

(d) with respect to the use and disposal of any property which at the commencement of this Act is held for the use of the said Court or of any officer of the said Court, and of any room or building which at that date is appropriated for the use of the said Court or of the Vice-Warden, officers, and suitors thereof ; and

(e) with respect to the custody of any records which at that date are under the custody of the said Court.

3.—References in any unrepealed enactment to mines subject to the jurisdiction of the Court of the Vice-Warden of the Stannaries, or within the cognisance of the said Vice-Warden, shall be construed as applying to mines which would have been subject to the jurisdiction of the said Court if it had not been abolished.

4.—(1) In the event of any dispute arising between :—

(a) any two or more mining companies ; or

(b) any mining company and any person having any estate or interest in the mine worked by or leased to that mining company ;

a Judge of a County Court exercising the jurisdiction of the Stannaries Court may, on the application of any party to the dispute, order that the matter in dispute be tried before himself or before an arbitrator agreed on by the parties or an officer of the Court, and the Arbitration Act 1889 shall apply to any such reference.

(2) For the purposes of this section the expression " mining company " shall mean any person or body of persons engaged in or formed for working mines within the Stannaries.

6.—This Act shall come into operation on the first day of January one thousand eight hundred and ninety-seven.

INSURANCE COMPANIES.

THE LIFE ASSURANCE COMPANIES ACT, 1870.

*33 and 34 Vict. c. 61.**Deposit.*

3.—Every company established after the passing of this Act within the United Kingdom, and every company established or to be established out of the United Kingdom which shall after the passing of this Act commence to carry on the business of life assurance within the United Kingdom, shall be required to deposit the sum of twenty thousand pounds with the Accountant-General of the Court of Chancery, to be invested by him in one of the securities usually accepted by the Court for the investment of funds placed from time to time under its administration, the company electing the particular security and receiving the income therefrom, and the Registrar shall not issue a certificate of incorporation unless such deposit shall have been made, and the Accountant-General shall return such deposit to the company so soon as its life assurance fund, accumulated out of the premiums, shall have amounted to forty thousand pounds.

Life Funds Separate.

4.—In the case of a company established after the passing of this Act, transacting other business besides that of Life Assurance, a separate account shall be kept of all receipts in respect of the life assurance and annuity contracts of the company, and the said receipts shall be carried to and for a separate fund to be called the Life Assurance Fund of the company, and such fund shall be as absolutely the security of the life policy and annuity-holders as though it belonged to a company carrying on no other business than that of Life Assurance, and shall not be liable for any contracts of the company for which it would not have been liable had the business of the company been only that of Life Assurance; and in respect to all existing companies, the exemption of the Life Assurance Fund from liability for other obligations than to its life policy holders shall have reference only to the contracts entered into after the passing of this Act, unless by the constitution of the company such exemption already exists. Provided always, that this section shall not apply to any contracts made by any existing company by the terms of whose deed of settlement the whole of the profits of all the business

are paid exclusively to the life policy holders, and on the face of which contracts the liability of the assured distinctly appears.

Statements to be made by Companies.

5.—From and after the passing of this Act every company shall, at the expiration of each financial year of such company, prepare a statement of its Revenue Account for such year, and of its Balance Sheet at the close of such year, in the forms respectively contained in the first and second schedules to this Act.

Statements by Company doing other than Life Business.

6.—Every company which, concurrently with the granting of policies of assurance or annuities on human life, transacts any other kind of assurance or other business shall, at the expiration of each such financial year as aforesaid, prepare statements of its Revenue Account for such year, and of its Balance Sheet at the close of such year, in the forms respectively contained in the third and fourth schedules of this Act.

Actuarial Report and Abstract.

7.—Every company shall, once in every five years if established after the passing of this Act, and once every ten years if established before the passing of this Act, or at such short intervals as may be prescribed by the instrument constituting the company, or by its regulations or bye-laws, cause an investigation to be made into its financial condition by an actuary, and shall cause an abstract of the report of such actuary to be made in the form prescribed in the fifth schedule to this Act.

Statement of Life and Annuity Business.

8.—Every company shall, on or before the thirty-first day of December, one thousand eight hundred and seventy-two, and thereafter within nine months after the date of each such investigation as aforesaid into its financial condition, prepare a statement of its life assurance and annuity business in the form contained in the sixth schedule of this Act, each of such statements to be made up as at the date of the last investigation, whether such investigation be made previously or subsequently to the passing of this Act : Provided as follows :—

(1) If the next financial investigation, after the passing of this Act, of any company fall during the year one thousand eight hundred and seventy-three, the said statement of such company shall be prepared within nine months after the date of such investigation, instead of on or before the thirty-first day of December, one thousand eight hundred and seventy-two.

(2) If such investigation be made annually by any company, such company may prepare such statement at any time, so that it be made at least once in every three years.

The expression "date of each such investigation" in this section shall mean the date to which the accounts of each company are made up for the purposes of each such investigation.

Forms may be altered.

9.—The Board of Trade, upon the application of or with the consent of a company, may alter the forms contained in the schedules of this Act, for the purposes of adapting them to the circumstances of such company, or of better carrying into effect the objects of this Act.

*Statements, etc., to be Signed and Printed and Deposited with Board
of Trade.*

10.—Every statement or abstract hereinbefore required to be made shall be signed by the chairman and two directors of the company and by the principal officer managing the life assurance business, and, if the company has a managing director, by such managing director, and shall be printed; and the original, so signed as aforesaid, together with three printed copies thereof, shall be deposited at the Board of Trade within nine months of the dates respectively hereinbefore prescribed as the dates at which the same are to be prepared. And every annual statement so deposited after the next investigation shall be accompanied by a printed copy of the abstract required to be made by section seven.

Copies of Statements to be given to Shareholders, etc.

11.—A printed copy of the last deposited statement, abstract, or other document by this Act required to be printed, shall be forwarded by the company by post or otherwise, on application, to every shareholder and policy-holder of the company.

FORM OF ANNUAL ACCOUNTS PRESCRIBED BY LIFE
ASSURANCE COMPANIES ACT, 1870.

FIRST SCHEDULE.

REVENUE ACCOUNT of the for the year ending 18 .

18 (Date)	Amount of Funds at the beginning of the year.. Premiums.. .. Consideration for Annu- ities granted Interest and Dividends Other Receipts (Accounts to be specified) ..	£ s d	18 (Date)	Claims under Policies (after deduction of Sums re-assured) .. Surrenders Annuities Commission Expenses of Manage- ment Dividends and Bonuses to Shareholders (if any) Other Payments (Ac- counts to be specified) Amount of Funds at the end of the year as per Second Schedule ..	£ s d
		£			£

Note 1.—Companies having separate Accounts for Annuities to return the particulars of their Annuity business in a separate statement.

Note 2.—Items in this and in the Accounts in the Third and Fifth Schedules should be the net amounts after deduction of the amounts paid and received in respect of re-assurances.

SECOND SCHEDULE.

BALANCE SHEET of the on the 18 .

<i>Liabilities.</i>	£ s d	<i>Assets.</i>	£ s d
Shareholders' Capital paid- up (if any) £		Mortgages on Property within the United Kingdom	
Assurance Fund		Mortgages on Property out of the United Kingdom	
Annuity Fund (if any)		Loans on the Company's Policies	
Other Funds (if any), to be specified		Investments—	
Total Funds as per First Schedule		In British Government Securi- ties	
Claims admitted but not paid* ..		Indian and Colonial Government Securities	
Other sums owing by the Company* (Accounts to be specified) ..		Foreign Government Securities	
		Railway and other Debentures and Debenture Stocks ..	
		Railway Shares (Preference and Ordinary)	
		House Property	
		Other Investments (to be speci- fied)	
		Loans upon Personal Security ..	
		Agents' Balances	
		Outstanding Premiums	
		Interest	
		Cash—On Deposit £	
		In hand and on Cur- rent Account	
		Other Assets (to be specified) ..	
	£		£

* *Note.*—These items are included in the corresponding items in the First Schedules.

THIRD SCHEDULE.

REVENUE ACCOUNTS of the _____ for the year ending _____.

No. 1.—LIFE ASSURANCE ACCOUNT.

(Date)	£ s d	(Date)	£ s d
Amount of Life Assurance Fund at the beginning of the year ..		Claims under Life Policies (after deduction of sums re-assured) ..	
Premiums, after deduction of Re-assurance Premiums		Surrenders	
Consideration for Annuities granted		Annuities	
Interest and Dividends ..		Commission	
Other Receipts (accounts to be specified) ..		Expenses of Management	
		Other Payments (accounts to be specified) ..	
		Amount of Life Assurance Fund at the end of the year, as per Fourth Schedule ..	
	£		£

Note.—Companies having separate Accounts for Annuities to return the particulars of their Annuity business in a separate statement.

No. 2.—FIRE ACCOUNT.

(Date)	£ s d	(Date)	£ s d
Amount of Fire Insurance Fund at the beginning of the year ..		Losses by fire (after deduction of Re-assurances)	
Premiums received after deduction of Re-assurances		Expenses of Management Commission	
Other Receipts, to be specified		Other Payments (to be specified)	
		Amount of Fire Insurance Fund at the end of the year, as per Fourth Schedule	
	£		£

Note.—When Marine or any other branch of business is carried on, the income and expenditure thereof to be in like manner stated in a separate account.

No. 3.—PROFIT AND LOSS ACCOUNT.

(Date)	£ s d	(Date)	£ s d
Balance of last year's Account		Dividends and Bonuses to Shareholders ..	
Interest and Dividends not carried to other accounts		Expenses not charged to other accounts	
Profits realised (accounts to be specified) ..		Loss realised (accounts to be specified)	
Other Receipts		Other Payments	
	£	Balance as per Fourth Schedule	
			£

Note.—This Account is not required if the items have been incorporated in the other accounts of this Schedule.

FOURTH SCHEDULE.

BALANCE SHEET of the

on the

18 .

<i>Liabilities.</i>	£ s d	<i>Assets.</i>	£ s d
Shareholders' Capital		Mortgages on Property within the	
General Reserve Fund (if any) ..		United Kingdom	
Life Assurance Fund*		Mortgages out of the United King-	
Annuity Fund (if any)*		dom	
Fire Fund		Loans on the Company's Policies	
Marine Fund		Investments—	
Profit and Loss (if any)		In British Government Securi-	
Other Funds (if any, to be specified)		ties	
£ s d		Indian and Colonial Securities	
Claims under Life Policies		Foreign Securities	
admitted, but not yet paid*		Railway and other Debentures	
Outstanding Fire Losses..		and Debenture Stocks	
Marine "		Railway Shares (Preference	
Other sums owing by the		and Ordinary)	
Company (accounts to be		House Property	
specified)		Other Investments (to be speci-	
		fied)	
		Loans upon Personal Security ..	
		Agents' Balances	
		Outstanding Premiums	
		Interest	
		Cash—On Deposit	£
		In hand and on	
		Current Account	
		Other Assets (to be specified) ..	
£		£	

* If the Life Assurance Fund is, in accordance with section 4 of this Act, a separate trust fund for the sole security of the Life Policy holders, a separate Balance Sheet for the Life Branch may be given in the form contained in Schedule 2. In other respects the Company is to observe the above form. See also note to Second Schedule.

FIFTH SCHEDULE.

STATEMENT RESPECTING THE VALUATION OF THE LIABILITIES UNDER
LIFE POLICIES AND ANNUITIES of the , to be made
by the Actuary.

(The answers should be numbered to accord with the numbers of the
corresponding questions.)

1. The date up to which the valuation is made.
2. The principles upon which the valuation and distribution of profits among the policy-holders are made, and whether these principles were determined by the instrument constituting the company, or by its regulations or bye-laws or otherwise.
3. The table or tables of mortality used in the valuation.
4. The rate or rates of interest assumed in the calculations.
5. The proportion of the annual premium income (if any) reserved as a provision for future expenses and profits. (If none, state how this provision is made.)

6. The Consolidated Revenue Account since the last valuation, or in case of a company which has made no valuation, since the commencement of the business. (This return should be made in the form annexed.)

7. The liabilities of the company under life policies and annuities at the date of the valuation, showing the number of policies, the amount assured, and the amount of premiums payable annually under each class of policies, both with and without participation in profits; and also the net liabilities and assets of the company, with the amount of surplus or deficiency. (These returns should be made in the form annexed.)

8. The time during which a policy must be in force in order to entitle it to share in the profits.

9. The results of the valuation, showing :—

- (1) The total amount of profit made by the company.
- (2) The amount of profit divided among the policy-holders, and the number and amount of the policies which participated.
- (3) Specimens of bonuses allotted to policies for £100 effected at the respective ages of 20, 30, 40, and 50, and having been respectively in force for five years, ten years, and upwards, at intervals of five years respectively, together with the amounts apportioned under the various modes in which the bonus might be received.

(FORM referred to under heading No. 6, in the Fifth Schedule.)

CONSOLIDATED REVENUE ACCOUNT of the for years
commencing and ending .

	£	s	d		£	s	d
Amount of Funds on 18 , the beginning of 				Claims under Policies (after de- duction of sums re-assured)			
Premiums (after deduction of Re- assurance Premiums)				Surrenders			
Consideration for Annuities granted				Annuities			
Interest and Dividends				Commission			
Other Receipts (Accounts to be specified)				Expenses of Management			
				Dividends and Bonuses to Share- holders (if any)			
				Other Payments (Accounts to be specified)			
				Amount of Funds on 18 , the end of the period as per First (or Third) Schedule			
	£				£		

(FORM referred to under heading No. 7, in Fifth Schedule.)

SUMMARY AND VALUATION OF THE POLICIES of the as at 18 .

DESCRIPTION OF TRANSACTIONS	PARTICULARS OF THE POLICIES FOR VALUATION				VALUATION			
	Number of Policies	Sums Assured and Bonuses	Office Yearly Premiums	Net Yearly Premiums, if ascertained	Value by the		Table,	
					Interest	per cent.		
					Sums Assured and Bonuses	Office Yearly Premiums	Net Yearly Premiums, if computed	Net Liability
ASSURANCES.								
I. <i>With participation in Profits.</i>								
For whole term of life								
Other Classes (to be specified) ..								
Extra Premiums payable								
Total Assurances with Profits								
II. <i>Without participation in Profits.</i>								
For whole term of life								
Other Classes (to be specified) ..								
Extra Premiums payable								
Total Assurances without Profit								
Total Assurances								
Deduct Re-assurances								
Net Amount of Assurances ..								
Adjustment (if any)								
ANNUITIES.								
Immediate								
Other Classes (to be specified) ..								
Total of the Results								

The term "extra premium" in this Act shall be taken to mean the charge for any risk not provided for in the minimum contract premium. If policies are issued in or for any country at rates of premium deduced from tables other than the European Mortality Tables adopted by the company, separate schedules similar in form to the above must be furnished.

(FORM referred to under heading No. 7, in Fifth Schedule.)

VALUATION BALANCE SHEET of as at 18 .

Dr.

Cr.

To Net Liability under Assurance and Annuity Transactions (as per Summary Statement provided in Schedule 5)	£	By Life Assurance and Annuity Funds (as per Balance Sheet, under Schedule 2 or 4) ..	£
Surplus (if any)	£	" Deficiency (if any)	£

SIXTH SCHEDULE.

STATEMENT OF THE LIFE ASSURANCE AND ANNUITY BUSINESS OF
the on the 18 .

(The answers should be numbered to accord with the number of the corresponding questions. Statements of re-assurances corresponding to the statements in respect of assurances under headings 2, 3, 4, 5, and 6, are to be given.)

1. The published table or tables of premiums for assurances for the whole term of life which are in use at the date above mentioned.

2. The total amount assured on lives for the whole term of life, which are in existence at the date above mentioned, distinguishing the portions assured with and without profits, stating separately the total reversionary bonuses, and specifying the sums assured for each year of life from the youngest to the oldest ages.

3. The amount of premiums receivable annually for each year of life, after deducting the abatements made by the application of bonuses, in respect of the respective assurances mentioned under heading No. 2, distinguishing ordinary from extra premiums.

4. The total amount assured under classes of assurance business other than for the whole term of life, distinguishing the sums assured under each class, and stating separately the amount assured with and without profits, and the total amount of reversionary bonuses.

5. The amount of premiums receivable annually in respect of each such special class of assurances mentioned under heading No. 4, distinguishing ordinary from extra premiums.

6. The total amount of premiums which has been received from the commencement upon all policies under each special class mentioned under heading No. 4, which are in force at the date above mentioned.

7. The total amount of immediate annuities on lives, distinguishing the amounts for each year of life.

8. The amount of all annuities other than those specified under heading No. 7, distinguishing the amount of annuities payable under each class, the amount of premiums annually receivable, and the amount of consideration money received in respect of each such class, and the total amount of premiums received from the commencement upon all deferred annuities.

9. The average rate of interest at which the life assurance fund of the company was invested at the close of each year during the period since the last investigation.

10. A table of minimum values (if any) allowed for the surrender of policies for the whole term of life, and for endowments and endowment

assurances, or a statement of the method pursued in calculating such surrender values, with instances of its application to policies of different standing, and taken out at various interval ages from the youngest to the oldest.

Separate statements to be furnished for business at other than European rates, together with a statement of the manner in which policies on unhealthy lives are dealt with.

GAS ACCOUNTS.

THE GAS WORKS CLAUSES ACT, 1847.

10 Vict. c. 15.

Profits to be Limited.

30.—The profits of the undertaking to be divided amongst the undertakers in any year shall not exceed the prescribed rate, or where no rate is prescribed they shall not exceed the rate of ten pounds in the hundred by the year on the paid-up capital in the undertaking, which in such case shall be deemed the prescribed rate, unless a larger dividend be at any time necessary to make up the deficiency of any previous dividend which shall have fallen short of the said yearly rate.

Reserved Fund.

31.—If the clear profits of the undertaking in any year amount to a larger sum than is sufficient, after making up the deficiency in the dividends of any previous year as aforesaid, to make a dividend at the prescribed rate, the excess beyond the sum necessary for such purpose shall from time to time be invested in Government or other securities; and the dividends and interest arising from such securities shall also be invested in the same or like securities, in order that the same may accumulate at compound interest until the fund so formed amounts to the prescribed sum, or if no sum be prescribed a sum equal to one-tenth of the nominal capital of the undertakers, which sum shall form a reserved fund to answer any deficiency which may at any time happen in the amount of divisible profits or to meet any extraordinary claim or demand which may at any time arise against the undertakers; and if such fund be at any time reduced it may thereafter be again restored to the said sum, and so from time to time as often as such reduction shall happen.

32.—Provided always that no sum of money shall be taken from the said fund for the purpose of meeting any extraordinary claim, unless it be first certified in England or Ireland by two justices, and in Scotland by the sheriff, that the sum so proposed to be taken is required for the purpose of meeting an extraordinary claim within the meaning of this or the special Act.

33.—When such fund shall, by accumulation or otherwise, amount to the prescribed sum, or one-tenth of the nominal capital of the company, as the case may be, the interest and dividends thereon shall no longer be invested, but shall be applied to any of the general purposes of the undertaking to which the profits thereof are applicable.

34.—If in any year the profits of the undertaking divisible among the undertakers shall not amount to the prescribed rate, such a sum may be taken from the Reserve Fund as with the actual divisible profits of such year will enable the undertakers to make a dividend of the amount aforesaid, and so from time to time as often as the occasion shall require.

Appointment of Inspectors.

35.—In England or Ireland the Court of Quarter Session, and in Scotland the sheriff, may, on the petition of any two gas ratepayers, within the limits of the special Acts, nominate and appoint some accountant or other competent person, not being a proprietor of any gasworks, to examine and ascertain at the expense of the undertakers (the amount of such expense to be determined by the said Court or sheriff) the actual state and condition of the concerns of the undertakers, and to make report thereof to the said Court at the then present or some following sessions, or to the sheriff; and the said Court or sheriff may examine any witnesses upon oath touching the truth of the said accounts, and matters therein referred to; and if it thereupon appear to the said Court or sheriff that the profits of the undertakers for the preceding year have exceeded the prescribed rate, the undertakers *shall*, in case the whole of the said reserved fund has been, and then remains, invested as aforesaid, and in case dividends to the amount hereinbefore limited had been paid, make such a rateable deduction in the rate for gas to be furnished by them as in the judgment of the said Court or sheriff shall be proper, but at such rates as, when reduced, shall ensure to the undertakers (regard being had to the amount of profit before received) a profit as near as may be to the prescribed rate.

36.—Provided always, that if, in the case of any petition so presented, it appears to the said Court or sheriff that there was no sufficient ground for presenting the same, the said Court or sheriff may, if they or he think fit, order the petitioner to pay the whole or any part of the costs of, or incident to, such petition (the amount thereof to be determined by the said Court or sheriff), and the costs so ordered to be paid shall be recoverable in the same way as damages are recoverable under this or the special Act.

37.—If the undertakers shall, for seven days after being required to produce to the said Court or sheriff, or to the said accountant or other person as aforesaid, any books of account or other books, bills, receipts, vouchers, or papers, relating to the pecuniary affairs of the undertakers,

refuse or neglect to produce such books, bills, receipts, vouchers, or papers, they shall forfeit the sum of one hundred pounds for every such refusal or wilful neglect, and the further sum of ten pounds for every day such refusal or wilful neglect shall continue after the expiration of the said seven days, such respective penalties to be recovered by any person who will sue for the same, with full costs of suit in any of the superior Courts.

Accounts to be Lodged, &c.

38.—With respect to the yearly receipts and expenditure of the undertakers, be it enacted, that the undertakers shall, in each year after they have begun to supply gas under the provisions of this or the special Act, cause an account in abstract to be prepared of the total receipts and expenditure of all rents or funds levied under the powers of this or the special Act for the year preceding, under the several distinct heads of receipt and expenditure, with a statement of the balance of such account, duly audited and certified by the chairman of the undertakers, and also by the auditors thereof, if any; and a copy of such annual account, if the gas-works be situated in England or Ireland, shall be transmitted, free of charge, to the clerk of the peace for the county in which the gas-works are situate, and if the gas-works be situated in Scotland, such copies shall be transmitted, free of charge, to the sheriff clerk of such county, and such transmission shall be made on or before the 31st day of January in each year, under a penalty of £20 for each default; and the copy of such account so sent to the said clerk of the peace or sheriff clerk shall be kept by him, and shall be open to inspection by all persons at all reasonable hours, on payment of one shilling for each inspection.

THE GAS WORKS CLAUSES ACT, 1871.

34 and 35 Vict. c. 41.

35.—The undertakers shall fill up and forward to the local authority of every district within the limits of the special Act, on or before the twenty-fifth day of March in each year, an annual statement of accounts made up to the thirty-first day of December then next preceding, as near as may be in the form and containing the particulars specified in Schedule B to this Act annexed.

The undertakers shall keep copies of such annual statement at their office, and sell the same to any applicant at a price not exceeding one shilling for each such copy.

The Board of Trade, with the consent of the undertakers, may alter the said forms for the purpose of adapting them to the conveniences of the undertaking, or of better carrying into effect the objects of this section.

SCHEDULE B.
Form of Annual Accounts.
The Gas Company.

Year ending 31st December 18 .
A.—STATEMENT OF SHARE CAPITAL, on the 31st December 18 .

1	2	3	4	5	6	7	8	9
Description of Capital	Maximum Dividend authorised	Number of Shares issued	Nominal Amount of Share	Called up per Share	Total paid up	Amount issued but not paid up	Remaining to be issued	Total Amounts authorised
	£ s d		£ s d	£ s d	£ s d	£ s d	£ s d	£ s d

B.—STATEMENT OF LOAN CAPITAL, on the 31st December 18 .

1	2	3	4	5
Description of Loan (Mortgage, Bond, Detenture, Stock, &c.)	Rate per cent. of Interest	Total Amounts borrowed at 31st December 18 .	Remaining to be borrowed	Total Amounts authorised
		£ s d	£ s d	£ s d
Total Share Capital paid up (see A.)				
" Loan	"	£	£	£
Total Capital received ..				
		£	£	£

C.—CAPITAL ACCOUNT for the year ended 31st December 18

	Expenditure 31st Dec. 18—		Expended this year		Total to 31st Dec. 18—		Received during Year 31st Dec. 18—	Total Receipts to 31st Dec. 18—	
	£	s d	£	s d	£	s d		£	s d
1. To Expenditure to 31st December 18							
<i>Since that Date.</i>									
2. To Lands acquired, including Law Charges ..									
3. " New Buildings, Manufacturing Plant, Machines, Storage Works, and other structures con- nected with manufacture ..									
4. " New Mains and Service Pipes (not being in place of old ones), including laying same, paving, and other works connected with dis- tribution ..									
5. " New Meters (not in place of old ones), including fixing ..									
6. " Cost of promoting special Act ..									
7. " Special Items (if any) ..									
Total Expenditure					
To Balance of Capital Account							
					£		Total ..	..	£

Balance carried to Profit and Loss Account, E.

Dr. E.—PROFIT AND LOSS ACCOUNT (NET REVENUE) for the year ended 31st December 18 Cr.

	£	s	d
1. To Amount carried to Reserve Fund Account, F (if any) from profits of 18			
2. " Interest on temporary Loans, and Moneys received in anticipation of Calls			
3. " Do. on Mortgages and Bonds accrued to 31st Dec. 18			
4. " Do. on Debenture Stock to do.			
5. " Half-year's Dividend on 1st Preferential to 30th June 18			
6. " Do. 2nd Preferential to do.			
7. " Do. on Ordinary Shares at per cent.			
" Balance of Net Profit to be carried to next Account subject to half-year's Dividends to 31st Dec. 18			
	£		

F.—RESERVED FUND ACCOUNT, for the year ended 31st December 18

	£	s	d
1. Amount (if any) carried to Profit and Loss Account, E, to make up deficiencies of Dividends to 31st Dec. 18			
2. Amount paid for extraordinary Claim or Demand (if any)			
3. Amount of Balance to be carried to next Account			
	£		

Like Accounts must be given for Depreciation Fund for works on Leaseholds (if any).

G.—STATEMENT OF COALS, during the year ended 31st December 18 .

Description of Coal	In Store 31st December 18		Received during year		Carbonized or used during year		In Store 31st December 18	
	Tons		Tons		Tons		Tons	
Common
Cannel

+74

H.—STATEMENT OF RESIDUAL PRODUCTS, for the year ended 31st December 18

Description of Residual	In Store 31st December 18 Estimated		Made during year Estimated		Used in Manufac- ture during year Estimated		Sold during year		In Store 31st December 18 Estimated	
Coke—Common, chaldrons of 36 bushels..								
" Cannel								
Breeze								
Tar, gallons								
Ammoniacal Liquor, butts of 108 gallons								

Dr.

I.—GENERAL BALANCE SHEET, on 31st December 18 .

Cr.

	£ s d			£ s d	
1. To CAPITAL ACCOUNT—			1. By Cash at Bankers	..	..
Balance at credit thereof (Account C)	2. " on Deposit or at Interest	..	..
2. " PROFIT AND LOSS ACCOUNT—			3. " Coals for Stock on hand, 31st December 18	..	..
Balance at credit thereof (Account E)	4. " Coke and Breeze, 31st December 18	..	..
3. " RESERVED FUND—			5. " Tar and other products	..	..
Balance at credit thereof (Account F)	6. " Sundry Stores	..	..
4. " DEPRECIATION FUND (for Works on Leasehold Lands)—			7. " Gas Meter Rental; balance of this account due to the		
Balance at credit thereof (Account)	Company on 31st December 18, less Deposits and Pre-		
5. " Unpaid Dividends	payments	..	..
6. " Interest accrued and unpaid on Mortgages, Bonds, and	Coke and other residuals, 31st December 18	..	..
Debenture Stock, and other Loans, to 31st Dec. 18	9. " Sundry Accounts, 31st December 18	..	..
7. " Sundry Tradesmen and others, for amount due for Coals,	" Special Items (if any), including Investments..	..	..
Stores, &c., to 31st December 18			
8. " WAGES AND CONTINGENCIES—					
Amount due to 31st December 18			
" Other Items (if any)			

£

£

AUDITING.

WATER ACCOUNTS.

THE WATERWORKS CLAUSES ACT, 1847.

*10 and 11 Vict. c. 17.**Profits of the Company to be limited.*

75.—The profits of the undertaking to be divided among the undertakers in any year shall not exceed the prescribed rate, or where no rate is prescribed they shall not exceed the rate of ten pounds in the hundred by the year on the paid-up capital in the undertaking, which in such case shall be deemed the prescribed rate, unless a larger dividend be at any time necessary to make up the deficiency of any previous dividend which shall have fallen short of the said yearly rate.

Reserved Fund.

76.—If the clear profits of the undertaking in any year amount to a larger sum than is sufficient, after making up the deficiency in the dividends of any previous year as aforesaid, to make a dividend at the prescribed rate, the excess beyond the sum necessary for such purpose shall from time to time be invested in Government or other securities, and the dividends and interest arising from such securities shall also be invested in the same or like securities, in order that the same may accumulate at compound interest until the fund so formed amounts to the prescribed sum, or if no sum be prescribed to a sum equal to one-tenth part of the nominal capital of the undertakers, which sum shall form a reserved sum to answer any deficiency which may at any time happen in the amount of divisible profits, or to meet any extraordinary claim or demand which may at any time arise against the undertakers; and if such fund be at any time reduced it may thereafter be again restored to the said sum, and so from time to time as often as such reduction shall happen.

77.—Provided always that no sum of money shall be taken from the said fund for the purpose of meeting any extraordinary claim, unless it be first certified, in *England or Ireland*, by two justices, and in *Scotland* by the sheriff, that the sum so proposed to be taken is required for the purpose of meeting any extraordinary claim within the meaning of this or the special Act.

78.—When such fund shall, by accumulation or otherwise, amount to the prescribed sum, or one-tenth part of the nominal capital, as the case may be, the interest and dividends thereon shall no longer be invested, but shall be applied to any of the general purposes of the undertaking to which the profits thereof are applicable.

79.—If in any year the profits of the undertaking divisible amongst the undertakers shall not amount to the prescribed rate, such a sum may be taken from the reserved fund as, with the actual divisible profits of such year, will enable the undertakers to make a dividend of the amount aforesaid, and so from time to time as often as the occasion shall require.

Annual Account to be sent to the Clerk of the Peace in England or Ireland, or to the Sheriff Clerk in Scotland, and to be open to Inspection.

83.—And with respect to the yearly receipt and expenditure of the undertakers, be it enacted, that the undertakers shall, in each year after they have begun to supply water under this or the special Act, cause an account in abstract to be prepared of the whole receipt and expenditure of all rates or other moneys levied under the powers of this or the special Act for the year preceding, under the several distinct heads of receipt and expenditure, with a statement of the balance of such account, duly audited and certified by the chairman of the undertakers, and also by the Auditors thereof, if any; and a copy of such annual account shall be sent, free of charge, to the clerk of the peace for the county in which the waterworks are situated, if the waterworks are situated in *England or Ireland*, and if the waterworks are situated in *Scotland*, to the sheriff clerk of such county, on or before the thirty-first day of *January* in each year, under a penalty of twenty pounds for each default and the copy of such account so sent to the said clerk shall be kept by him, and shall be open to inspection by all persons, at all reasonable hours, on payment of one shilling for each inspection.

METROPOLIS WATER ACT, 1902.

2 Edw. 7, c. 41.

Establishment of Water Board.

1.—(1) A board, to be called the Metropolitan Water Board, and in this Act, referred to as "the Water Board," shall be established for the purpose of acquiring by purchase and of managing and carrying on the undertakings of the companies mentioned in the first schedule to this Act (in this Act referred to as "metropolitan water companies"), and generally for the purpose of supplying water within the area described in the second schedule to this Act, subject to such alterations therein as may be made by or under this Act (which area is in this Act referred to as "the limits of supply").

(2) The Water Board shall be a body corporate with a common seal, having power to acquire and hold land for the purposes of this Act without licence in mortmain.

Financial Provisions.

15.—(1) There shall be established a water fund, and all receipts of the Water Board shall be carried to that fund, and all payments by the Board shall be made out of that fund.

(2) Any sum required to meet any deficiency in the water fund, whether for satisfying past or future liabilities, in any financial year, shall be apportioned amongst the City of London and the metropolitan boroughs in the County of London and the municipal boroughs and urban districts outside London, the councils of which are for the time being entitled to be represented on the Water Board, in proportion to the rateable value appearing in the valuation lists in force on the preceding sixth day of April of the hereditaments at that date supplied with water by the Water Board or any metropolitan water company or the council of the urban district of Tottenham or Enfield in the City and each such borough and district.

(3) The Water Board shall issue precepts for the sums apportioned to the City and the several boroughs and districts liable—

- (a) in the case of the City of London, to the common council ;
- (b) in the case of a metropolitan borough, to the council of that borough ;
- (c) in the case of a municipal borough or urban district, to the council thereof ;

and the council shall pay to the Water Board the amount specified in the precept.

(4) The amount required by any such precept shall be paid—

- (a) in the case of the city out of the consolidated rate ;
- (b) in the case of a metropolitan borough as part of the expenses incurred by the council thereof ;
- (c) in the case of a municipal borough or urban district out of the fund or rate out of which the expenses of the council thereof incurred in the execution of the Public Health Acts are payable.

(5) A demand note for any rate levied for defraying any expenses of the Water Board, together with other expenses, shall state as a separate item the amount to be paid for defraying the expenses of that Board.

(6) The Water Board shall not, until Parliament otherwise determine, reduce the rates charged for the supply of water below those in force during the quarter ending the twenty-fourth day of June one thousand nine hundred and two, unless the Board are satisfied that such a reduction would not cause a deficiency in the water fund ; but the Water Board

shall, within three years after the appointed day, introduce into Parliament a Bill providing for uniform scales of charges applicable throughout the limits of supply.

(7) Within three years after the appointed day the Water Board may prepare and publish in the *London Gazette* a scheme enabling their charges for the supply of water to be collected together with any local rate.

Any local or rating authority within the limits of supply may transmit to the Local Government Board their objections to any such scheme within forty days after the scheme is published in the *London Gazette*.

16.—(1) The Water Board may borrow money for the purpose of—

- (a) paying any money (other than money payable by way of interest on purchase money) payable under this Act by the Water Board to a metropolitan water company ; and
- (b) paying any money payable under this Act by the Water Board to the council of the urban district of Tottenham or Enfield ; and
- (c) purchasing, redeeming, or paying off any debenture stock or mortgage debt ; and
- (d) executing any work authorised by the Acts relating to any of the metropolitan water companies, so that the amount does not exceed the amounts which were immediately before the appointed day under those Acts authorised to be raised for that purpose, but have not been raised before that date ; and
- (e) paying any compensation payable under this Act (otherwise than by way of annuity) ;

and, with the consent of the Local Government Board, for the purpose of any payment by the Water Board or of any permanent work or other thing which the Water Board are authorised to execute or do, and which or the cost of which ought, in the opinion of the Local Government Board, to be spread over a term of years.

(2) All money borrowed under this section shall be raised by means of the issue of water stock under this Act, unless the Local Government Board consent to some other mode of raising the money, and, where the Local Government Board so consent, any money raised and the interest thereon shall be charged on the water fund or on such property or revenues of the Water Board, and in such manner as the Local Government Board may sanction.

(3) Any money borrowed under this Act, if borrowed for the purpose of making any payment to a metropolitan water company, or to the council of the urban district of Tottenham or Enfield, or of redeeming, purchasing, or paying off any debenture stock or mortgage debt, shall be repaid within the period of one hundred years from the thirty-first day of March one thousand nine hundred and three, and, if borrowed for any other purpose shall be repaid within such period not exceeding sixty years from the date of the borrowing as the Water Board, with the consent of the Local Government Board, may determine.

(4) For the purpose of paying off a loan raised under this Act, the Water Board shall have the like powers of reborrowing as a county council have under section sixty-nine of the Local Government Act 1888, and the provisions of that section so far as they relate to reborrowing shall apply as if they were herein re-enacted and in terms made applicable to the Water Board and to the security on which that Board are by or under this Act authorised to borrow.

(5) So much of any Local Act as relates to the method of borrowing money by a metropolitan water company shall as from the appointed day be repealed.

17.—(1) For the purpose of enabling the Water Board to raise money which they are authorised to borrow under this Act, and to issue any water stock which, under the provisions of this Act, is to be issued to any metropolitan water company or the holder of any debenture stock or mortgage debt, the Water Board may create a sufficient amount of stock, to be called Metropolitan Water Stock, and in this Act referred to as water stock, bearing interest at such a rate not exceeding three pounds per centum per annum, as the Water Board, with the consent of the Local Government Board, and after consultation with the Governor of the Bank of England, may resolve.

(2) Water stock and the interest thereon shall be charged on the water fund and all on the revenues of the Water Board.

(3) Subject to the provisions of this Act, the provisions of section fifty-two of the Public Health Acts Amendment Act 1890, which relates to the issue of stock by local authorities, shall apply to water stock as if it were stock created under, and the Water Board were an authority mentioned in, that section, and the regulations in respect of water stock issued to the holders of irredeemable debenture stock shall be uniform with the regulations in respect of other water stock except as to the period of redemption and the provisions relating thereto.

(4) Water stock shall be included amongst the securities in which a trustee may invest under the powers of the Trustee Act 1893.

18.—(1) The Water Board shall, in accordance with regulations made by the Local Government Board, by the creation of one or more sinking or redemption funds or otherwise, make provision for—

- (a) the discharge within a period of one hundred years from the thirty-first day of March one thousand nine hundred and three of the amount of any water stock issued by the Board in consideration for the undertaking of any metropolitan water company or in substitution or in consideration for any debenture stock or mortgage debts ; and
- (b) the discharge within that period of all debenture stock and mortgage debts which under this Act are to be discharged within that period ; and
- (c) the discharge within the periods within which they are under this Act to be discharged of any sums borrowed by the Water Board under this Act :

Provided that during the first twenty years of the said period of one hundred years the Water Board shall not be required to make any payments towards the discharge of water stock, debenture stock, mortgage debts, or loans, for the discharge of which the said period of one hundred years is fixed by this Act, other than the payment in respect of each year towards the discharge of such water stock of the amount (if any) by which the receipts on Revenue Account exceed the expenditure on that account of the Water Board in that year, after deducting such sum as may be reasonably necessary for meeting current expenses. The sums so to be paid shall be paid as soon as may be after the amount thereof is ascertained, and the certificate of the Auditor of the accounts of the Water Board, subject to such variations as the Local Government Board may allow, shall be conclusive as to the amount to be paid.

(2) The Local Government Board may make regulations under this Section, and the regulations so made—

- (a) if they relate to the discharge of water stock, shall be made under section fifty-two of the Public Health Acts Amendment Act 1890, as applied by this Act ; and
- (b) if they relate to the discharge of any debenture stock, mortgage debts, or loans, may apply, with or without modifications, any enactments of the Local Loans Act 1875, and the Acts amending that Act, and may contain such other provisions as appear to the Local Government Board necessary or proper for the purpose of the regulations, and shall have effect as if they were enacted in this Act.

(3) For the purpose of this section, the expression "discharge" means—

- (a) with respect to water stock and debenture stock, the redemption or purchase thereof ; and
- (b) with respect to mortgage debts and loans, the payment off or repayment thereof.

19.—The accounts of the Water Board, and any committee appointed by them, and of their officers, shall be made up and audited in like manner, and subject to the same provisions, as the accounts of county councils, except that a water consumer shall have the same right of being present at the audit, and of making objections and appealing, as a rate-payer has, and that the stamp duty charged on the Water Board for the purposes of the District Auditors Act 1879, shall be such as the Treasury, after consultation with the Local Government Board, and having regard to the cost of the audit, may determine, and the enactments relating to the accounts of county councils and the audit thereof, and to all matters incidental thereto and consequential thereon, including the penal provisions, shall apply accordingly.

20.—(1) At the beginning of every financial year the Water Board shall cause to be submitted to them an estimate of the receipts and expenditure of such Board during that financial year whether on account of property, contributions, rates, loans, or otherwise.

(2) All payments to and out of the water fund shall be made to and by the treasurer of the Water Board, and all payments out of the fund shall be made in pursuance of an order of the Water Board signed by three members of the finance committee present at the meeting of the Board and countersigned by the clerk of the Board, and the same order may include several payments.

Moreover all cheques for the payment of money issued in pursuance of such order shall be countersigned by the clerk of the Board, or by a deputy approved by the Board.

(3) The Water Board shall from time to time appoint a finance committee for regulating and controlling their finance, and an order for the payment of a sum out of the water fund whether on account of capital or income shall not be made by the Water Board except in pursuance of a resolution of the Board passed on the recommendation of the finance committee, and any costs, debt, or liability exceeding fifty pounds shall not be incurred except upon a resolution of the Board passed on an estimate submitted by the finance committee.

(4) The notice of the meeting at which any resolution for the payment of a sum out of the water fund (otherwise than for ordinary periodical payments), or any resolution for incurring any costs, debt, or liability exceeding fifty pounds, will be proposed, shall state the amount of the said sum, costs, debt, or liability and the purposes for which they are to be paid or incurred.

21.—(1) The payment of any money payable by a local authority to the Water Board in respect of any waterworks and plant transferred to the authority by or under this Act or in respect of the right to supply water within any part of the area of the authority shall for purposes of borrowing be deemed to be expenses incurred by the authority in the execution of the Public Health Acts.

(2) The amount of money to be borrowed shall not be restricted by the limitation on borrowing contained in subsections (2) and (3) of section two hundred and thirty-four of the Public Health Act 1875, and in calculating the amount which the local authority may borrow under the last-mentioned Act any money borrowed by the authority for the purposes of this Act shall not be reckoned.

22.—Any money received by the Water Board from the Chamberlain of the City of London under this Act, or in respect of any waterworks and plant transferred from the Board by or under this Act, or as the proceeds of the sale of any land under this Act, and any other capital receipts of the Board, not applicable to any other purpose, shall be applied in such manner as the Local Government Board sanction towards any purpose for which money may be borrowed under this Act, or towards the discharge of any loan, or otherwise for any purpose for which capital money may be applied by the Water Board.

28.—The Water Board shall make to the Local Government Board an annual report of their proceedings, and this report shall be laid annually before Parliament by the Local Government Board. The Water Board shall also give to the Local Government Board such returns, statistics, and information, with respect to the exercise of the powers of the Water Board, as the Local Government Board may require.

48.—(1) The Water Board shall pay to each of the metropolitan water companies, by way of compensation for the loss of office sustained by such of the directors of the company as were in office both at the date of the publication of the notice of the Bill for this Act and on the appointed day, such sum as may be agreed upon between the Water Board and the company, or, in default of agreement, as may be determined by an arbitrator appointed by the Local Government Board.

(2) The sum paid to any company under this section shall be distributed amongst the directors entitled to compensation in such proportions as those directors, or a majority of them, determine.

49.—The Water Board shall pay to the Auditor of the accounts of the metropolitan water companies such annual or other sum by way of compensation for loss of office as the Local Government Board may think just.

ELECTRIC LIGHTING ACCOUNTS.

ELECTRIC LIGHTING ACT, 1882.

45 and 46 Vict. c. 56.

9.—The undertakers shall, on or before the twenty-fifth day of March in every year, fill up an annual statement of accounts of the undertaking made up to the thirty-first day of December then next preceding; and such statement shall be in such form and shall contain such particulars and shall be published in such manner as may from time to time be prescribed in that behalf by the Board of Trade.

The undertakers shall keep copies of such annual statement at their office and sell the same to any applicant at a price not exceeding one shilling a copy.

ELECTRIC LIGHTING ACTS, 1882 TO 1890.
Form of Accounts prescribed by the Board of Trade for an Electric Lighting Company.
ELECTRIC LIGHTING ORDER (LICENCE).

THE
 COMPANY.

Year ending 31st December 18 . . .

STATEMENT OF SHARE CAPITAL APPROPRIATED FOR THE PURPOSES OF THE UNDERTAKING
 AUTHORISED BY THE ABOVE-MENTIONED ORDER (LICENCE).

No. I.

On the 31st December 18 . . .

Description of Capital	Authorised by	Number of Shares Issued	Nominal Amount of Share	Called-up per Share	Total Paid-up	Issued not Paid-up	Remaining Un-issued	Total Amount Authorised

AUDITING.

STATEMENT OF LOAN CAPITAL APPROPRIATED FOR THE PURPOSES OF THE UNDERTAKING
AUTHORISED BY THE ABOVE-MENTIONED ORDER (LICENCE).

No. II.

on the 31st December 18 .

Description of Loan	Amounts borrowed			Remaining Borrowing Powers	Total amount of Borrowing Powers
	At per cent.	At per cent.	Total		

Total Share Capital paid-up, see No. I. £
 " Loan " borrowed, see No. II. £
 Total Capital received £

Dr.

CAPITAL ACCOUNT

for the year ending 31st December 18 .

No. III.

	Expenditure up to 31 Dec. 18		Expended during the Year.		Total Expenditure to 31 Dec. 18		Receipts up to 31 Dec. 18		Received during Year.		Total Receipts to 31 Dec. 18	
	£	s d	£	s d	£	s d	£	s d	£	s d	£	s d
To Expenditure to 31st December 18										
<i>Expenditure since that date.</i>												
1. To Lands, including Land Charges incidental to Acquisition					By Ordinary Shares of £	..	..	..	..	..
2. " Buildings					" " " £
3. " Machinery					" Preference " £	..	..	..	..	..
4. " Accumulators at Generating and Distributing Stations					" Debenture Stock £	..	..	..	..	..
5. " Mains, including Cost of Laying the Mains					" Mortgages and Bonds ..	..	..	..	..	..
6. " Transformers, Motors, &c.					" Amounts received in anticipation of Calls	..	..	..	..	..
7. " Meters, and Fees for Certifying under the Act					" Sale of Patents or Patent Rights, &c. ..	..	..	..	..	..
8. " Electrical Instruments, &c.					" Other Receipts (to be specified) ..	..	..	..	..	..
9. " General Stores (Cables, Mains, Lamps)										
10. " Purchase of Patents or Patent Rights										
11. " Cost of Licence, Provisional Order, &c.										
12. " Special Items										
Total Expenditure										
To Balance of Capital Account										

Provision for Depreciation of Works is made by a debit of £ to Revenue Account transferred to Depreciation Fund Account, No. VII.

No. IV. *Dr.* for the year ending 31st December 18

ELECTRIC LIGHTING ACT, 1882.

487

A.—To Generation of Electricity.		£	s	d	£	s	d
1. To Coals or other Fuel, including Dues, Carriage, Unloading, Storing, and all Expenses of placing the same on the Works							
2. " Oil, Waste, Water, and Engine-room Stores							
3. " Proportion of Salaries of Engineers, Superintendents, and Officers, as certified by the Managing Director, Chairman, or Engineer							
4. " Wages and Gratuities at Generating Stations							
5. " Repairs and Maintenance, as follows:—							
1. Buildings	£	s	d				
2. Engines, Boilers							
3. Dynamos, Exciters, Transformers, Motors, &c.							
4. Other Machinery, Instruments, and Tools							
5. Accumulators and Accessories							
Less Received for Old Material							
6. " Special Items							
B.—To Distribution of Electricity.							
1. To Proportion of Salaries of Superintendents and Officers, as certified by Managing Director, Chairman, or Engineer							
2. " Wages and Gratuities to Linesmen, Fitters, Labourers							
3. " Repairs, Maintenance, and Renewals of Mains of all classes, including Materials and laying the same							
Less Amounts Refunded							
4. " Repairs, Maintenance, and Renewal of Transformers, Meters, Switches, Fuses, and other Apparatus on Consumers' Premises							
5. " Repairs, Maintenance, and Renewals of Apparatus at Distributing Stations							
Carried forward							
1. By Sale of Current per meter at per B. T. U. ..							
2. " Sale under Contracts							
3. " Public Lighting							
4. " Rental of Meters and other Apparatus on Consumers' Premises							
5. " Sale and Repairs of Lamps, Arc or Incandescent Sale and Repairs of other Apparatus							
6. " Royalties, Licences, &c.							
7. " Rents Receivable							
8. " Transfer Fees							
9. " Other Items (to be specified)							
Carried forward							

Dr.

No. IV.—*continued.*REVENUE ACCOUNT—*continued.*

Cr.

	£	s	d	£	s	d	£	s	d
Brought over									
C.— <i>To Public Lamps.</i>									
1. To Attending and Repairs									
2. " Renewals of Lamps									
D.— <i>To Royalties, &c.</i>									
To Royalties, &c., Payable for use of Patents or Patent Processes									
E.— <i>To Rents, Rates, and Taxes.</i>									
1. To Rents Payable.									
2. " Rates and Taxes									
F.— <i>To Management Expenses.</i>									
1. To Directors' Remuneration.									
2. " Salaries of Managing Engineers, Secretary, Accountants, Clerks, Messengers, as certified by Managing Director, Chairman, or Engineer									
3. " Salaries or Commissions of Collectors									
4. " Stationery and Printing									
5. " General Establishment Charges									
6. " Auditors of Company									
7. " Auditor appointed under the Provisions of the Order									
G.— <i>To Law and Parliamentary Charges.</i>									
To Law Expenses									
H.— <i>To Depreciation.</i>									
1. To Depreciation in respect of Leasehold Works									
2. " Do. Buildings									
3. " Do. Plant, Machinery, &c.									
I.— <i>To Special Charges.</i>									
1. To Insurance, Superannuation, &c.									
2. " Expenses for Certification of Meters									
Total Expenditure									
Balance carried to Net Revenue									

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AUDITING.

£

£

NET REVENUE ACCOUNT.

Cr.

	£	s	d
To Interest on Debentures accrued due to date			
" " Interest on Mortgages and Bonds accrued due to date			
" " Interest on Temporary Loans accrued due to date			
" " Dividend on Preference Stocks			
" " Balance applicable to Dividend on Ordinary Stock or Shares			
	£	s	d
1. By Balance from last Account			
Less Dividend paid			
" Amount carried to Reserve Fund			
2. By Balance brought from Revenue Account			
(No. IV.)			
3. " Interest on Money at Deposit			
	£	s	d
	£	s	d

RESERVE FUND ACCOUNT.

Cr.

	£	s	d
1. Amount paid out for
2. Amount of Balance to next Account
	£		
	£		

DEPRECIATED FUND ACCOUNT.

Cr.

	£	s	d
1. To Balance..
2. By Balance from last Account
3. " Interest on Investments
3. " Amount brought from Revenue Account (see No. IV. H.).
(Descriptions of Investments to be specified)			
			£

Dr.

No. V.

Dr.

No. VI.

Dr.

No. VII.

Dr.

GENERAL BALANCE SHEET.

Cr.

No. VIII.

<i>Liabilities</i>		£ s d	
1. To Capital Account : Amount received as per Account No. III.	£	s d
2. " Sundry Tradesmen and others, due on construction of Plant and Machinery, Fuel, Stores, &c., to 31 December 18	£	s d
3. " Sundry Creditors on open Accounts		
4. " Net Revenue Account : Balance at credit thereof		
5. " Reserve Fund Account :		
6. " Depreciation Fund Account :		
		£	
<i>Assets</i>		£ s d	
1. By Capital Account : Amount expended for Works as per Account No. III.	£	s d
2. " Stores on hand at 31st December 18 :—		
Coal		
Oils, Waste, &c.		
General		
3. " Sundry Debtors for amounts paid on account of Contract in course of completion		
4. " Preliminary Expenses		
5. " Sundry Debtors for Current supplied to 31st December 18		
6. " Other Debtors		
7. " Cash at Bankers :—		
Messrs.		
Messrs.		
Messrs.		
8. " Cash in hand		
		£	

Chairman,

Manager and Secretary.

March 18 .

ELECTRIC LIGHTING CLAUSES ACT, 1899.

62 and 63 Vict. c. 19.

1.—The provisions contained in the schedule to this Act shall be incorporated with and form part of every provisional order made by the Board of Trade after the commencement of this Act under the Electric Lighting Acts, save so far as they are expressly varied or excepted by the order, and shall, subject to any such variations or exceptions, apply, so far as applicable, to the undertaking authorised by the order. The said provisions shall also, with the necessary modifications, and, in particular, with the substitution of the words "special Act" for "special order" be incorporated with any special Act, save so far as they are expressly varied or excepted thereby. . . . The expression "special Act" means, in this Act, any Act passed after the commencement of this Act authorising the supply of electricity for any public or private purposes within any area.

2.—(2) Except so far as any of the provisions contained in the schedule to this Act are incorporated with any provisional order made by the Board of Trade under the Electric Lighting Acts extending to the county of London, or with any special Acts so extending, this Act shall not apply to the county of London.

Audit of Accounts.

6.—The following provisions shall apply as to the audit of accounts where the undertakers are not a local authority :—

(1) The annual statement of accounts of the undertaking, before being published as provided by section nine of the Electric Lighting Act 1882 shall be examined and audited by such competent and impartial person as the Board of Trade appoint, and the remuneration of the Auditor shall be such as the Board of Trade direct, and that remuneration and all expenses incurred by him in or about the execution of his duties, to such an amount as the Board of Trade approve, shall be paid by the undertakers on demand, and shall be recoverable summarily as a civil debt.

(2) The undertakers shall give to the Auditor, his clerks and assistants, access to such of the books and documents relating to the undertaking as are necessary for the purposes of the audit, and shall when required furnish to him and them all vouchers and information requisite for that purpose, and shall afford to him and them all facilities for the proper execution of his and their duty.

(3) The Board of Trade may make and vary regulations prescribing the times at and the mode in which the audit shall be made and con-

ducted, or otherwise for the purpose of giving effect to the provisions of this section.

(4) Any report made by the Auditor, or such portion thereof as the Board of Trade direct, shall be appended to the annual statement of accounts, and shall form part thereof for the purposes of the said section nine.

RAILWAY ACCOUNTS.

THE RAILWAY COMPANIES SECURITIES ACT, 1866.

29 and 30 Vict. c. 108.

2.—In this Act the term "railway" includes a tramway authorised by Act of Parliament incorporating the Companies Clauses Consolidation Act 1845, but not any other tramway :

The term "railway company" includes every company authorised by Act of Parliament to raise any loan capital for the construction or working of a railway, or for any purposes connected with the conveyance by such a company of traffic on a railway either alone or in conjunction with other purposes :

The term "debenture stock" includes mortgage preference stock and funded debt and any stock or shares representing loan capital of a railway company, by whatever name called.

Half-yearly Accounts.

4.—Half-years shall, for the purpose of this Act, be deemed to end on the thirtieth day of June and the thirty-first day of December ; and the first half-year to which this Act applies shall be that ending on the thirty-first day of December one thousand eight hundred and sixty-six ; but the Board of Trade, on the application of any railway company, may (by writing under the hand of one of their secretaries or assistant secretaries, which shall be registered by the railway company at the office of the said Registrar) appoint, with respect to that company, other days for the ending of half-years (including the first).

5.—Within fourteen days after the end of each half-year every railway shall make an account of their loan capital authorised to be raised and actually raised up to the end of that half-year, specifying the particulars described in the first schedule to this Act, Part 1 (which account for each half-year is in this Act referred to as the loan capital half-yearly account).

Form of Accounts.

6.—The Board of Trade may, from time to time, by notice published in the London, Edinburgh, and Dublin *Gazettes*, prescribe the form in which the loan capital half-yearly account is to be made.

THE FIRST SCHEDULE.

PART I.—PARTICULARS TO BE SPECIFIED IN LOAN CAPITAL
HALF-YEARLY ACCOUNT.

A.—Every half-yearly account to show—

(1) The Act or Acts of Parliament under the powers of which the company have contracted any mortgage or bond debt existing at the end of the half-year, or have issued any debenture stock then existing, or the Act or Acts of Parliament by or under which any mortgage or bond debt or debenture stock of the company then existing has been confirmed, and the Act or Acts of Parliament under which the company have any subsisting power to contract any mortgage or bond debt, or to issue any debenture stock (either on fulfilment of any condition or otherwise).

(2) The amount or respective amounts of mortgage or bond debt or debenture stock thereby authorised or confirmed.

(3) Whether or not by any such Act or Acts the obtaining of the certificate of a justice or sheriff for any purpose, or the obtaining of the assent of a meeting of the company, has been made a condition precedent to the exercise of the power thereby conferred of borrowing on mortgage or bond, or of creating and issuing debenture stock.

(4) The date at which such condition has been fulfilled.

(5) The amount or the aggregate amount under the powers of such Act or Acts actually borrowed up to the end of the half-year on mortgage or bond (distinguishing them), and then being an existing debt, and of debenture stock actually issued up to that time and then existing.

(6) The amount or the aggregate amount remaining to be borrowed.

B.—The second and every subsequent half-yearly account to show also—

(7) The items described in paragraphs (2) and (5) of this part of the present schedule for two consecutive half-years, and the increase or decrease of any of these items in the second of those half-years as compared with the first.

THE RAILWAY COMPANIES (SCOTLAND)
ACT, 1867.

30 and 31 Vict. c. 126.

Audit of Railway Accounts.

30.—No dividend shall be declared by a company until the Auditors have certified that the half-yearly accounts proposed to be issued contain a full and true statement of the financial condition of the company, and that the dividend proposed to be declared on any shares is *bonâ fide* due thereon after charging the revenue of the half-year with all expenses which ought to be paid thereout in the judgment of the Auditors; but if the directors differ from the judgment of the Auditors with respect to the payment of any such expenses out of the income of the half-year, such difference shall, if the directors desire it, be stated in the report to the shareholders, and the company in general meeting may decide thereon, subject to all the provisions of the law then existing, and such decision shall, for the purposes of dividend, be final and binding; but if no such difference is stated, or if no decision is given on any such difference, the judgment of the Auditors shall be final and binding; and the Auditors may examine the books of the company at all reasonable times, and may call for such further accounts, and such vouchers, papers, and information as they think fit, and the directors and officers of the company shall produce and give the same as far as they can, and the Auditors may refuse to certify as aforesaid until they have received the same; and the Auditors may at any time add to their certificate, or issue to the shareholders independently, at the cost of the company, any statement respecting the financial condition and prospects of the company which they think material for the information of the shareholders.

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THE RAILWAY COMPANIES ACT, 1867.

30 and 31 Vict. c. 127

Audit of Railway Accounts.

30.—No dividend shall be declared by a company until the Auditors have certified that the half-yearly accounts proposed to be issued contain a full and true statement of the financial condition of the company, and that the dividend proposed to be declared on any shares is *bonâ fide* due thereon after charging the revenue of the half-year with all expenses which ought to be paid thereout in the judgment of the Auditors; but if the directors differ from the judgment of the Auditors with respect

to the payment of any such expenses out of the revenue of the half-year, such difference shall, if the directors desire it, be stated in the report to the shareholders, and the company in general meeting may decide thereon, subject to all the provisions of the law then existing, and such decisions shall for the purpose of the dividend be final and binding; but if no such difference is stated, or if no such decision is given on any such difference, the judgment of the Auditors shall be final and binding; and the Auditors may examine the books of the company at all reasonable times, and may call for such further accounts, and such vouchers, papers, and information as they think fit, and the directors and officers of the company shall produce and give the same as far as they can, and the Auditors may refuse to certify as aforesaid until they have received the same; and the Auditors may at any time add to their certificate, or issue to the shareholders independently, at the cost of the company, any statement respecting the financial condition and prospects of the company which they think material for the information of the shareholders.

THE REGULATION OF RAILWAYS ACT, 1868.

31 and 32 Vict. c. 119.

Uniform Accounts, &c., to be kept.

3.—Every incorporated company, seven days at least before each ordinary half-yearly meeting held after the thirty-first day of *December* one thousand eight hundred and sixty-eight, shall prepare and print, according to the forms contained in the first schedule to this Act, a statement of accounts and Balance Sheet for the last preceding half-year, and the other statements and certificates required by the same schedule, and an estimate of the proposed expenditure out of capital for the next ensuing half-year, and such statement of accounts and Balance Sheet shall be the statement of accounts and Balance Sheet which are submitted to the Auditors of the company. Every company which makes default in complying with this section shall be liable to a penalty not exceeding five pounds for every day during which such default continues. The Board of Trade, with the consent of a company, may alter the said forms as regards such company for the purpose of adapting them to the circumstances of such company, or of better carrying into effect the objects of this section.

Accounts, &c., to be Signed, and Printed Copies Distributed.

4.—Every statement of accounts, Balance Sheet, and estimate of expenditure, prepared as required by this Act, shall be signed by the chairman or deputy chairman of the directors and by the accountant or

other officer in charge of the accounts of the company, and shall be preserved at the company's principal office. A printed copy thereof shall be forwarded to the Board of Trade.

Penalty for Falsifying Accounts, &c.

5.—If any statement, Balance Sheet, estimate, or report which is required by this Act is false in any particular to the knowledge of any person who signs the same, such person shall be liable, on conviction thereof on indictment, to fine and imprisonment, or on summary conviction thereof to a penalty not exceeding fifty pounds.

Auditor not necessarily a Shareholder.

11.—Whenever, after the passing of this Act, section one hundred and two of the Companies Clauses Consolidation Act 1845 is incorporated in a certificate or special Act relating to a railway company, it shall be construed as if the words, "where no qualification shall be prescribed by the special Act every Auditor shall have at least one share in the undertaking," were omitted therefrom; and so much of every certificate and special Act relating to a railway company, and in force at the passing of this Act, as incorporates that portion of the said section, and so much of any special Act relating to a railway company, and so in force as contains a like provision, is hereby repealed.

Auditors of Company, and appointment of Auditor by Board of Trade.

12.—With respect to the Auditors of the company the following provisions shall have effect:—

(1) The Board of Trade may, upon application made in pursuance of a resolution passed at a meeting of the directors or at a general meeting of the company, appoint an Auditor in addition to the Auditors of such company, and it shall not be necessary for any such Auditor to be a shareholder in the company;

(2) The company shall pay to such Auditor appointed by the Board of Trade such reasonable remuneration as the Board of Trade may prescribe;

(3) The Auditor so appointed shall have the same duties and powers as the Auditors of the company, and shall report to the company;

(4) Where, in consequence of such appointment of an Auditor or otherwise, there are three or more Auditors, the company may declare a dividend if the majority of such Auditors certify in manner required by Section 30 of the Railway Companies Act 1867, and the Railway Companies (Scotland) Act 1867, respectively;

(5) Where there is a difference of opinion among such Auditors the Auditor who so differs shall issue to the shareholders, at the cost of the company, such statement respecting the grounds on which he differs from his colleagues, and respecting the financial condition and prospects of the company, as he thinks material for the information of the shareholders.

Issue of Preferred and Deferred Ordinary Stock.

13.—Any company which, in the year immediately preceding, has paid a dividend on their ordinary stock of not less than three pounds *per centum per annum* may, pursuant to the resolution of an extraordinary general meeting, divide their paid-up ordinary stock into two classes, to be and to be called, the one preferred ordinary stock, and the other deferred ordinary stock, and issue the same subject and according to the following provisions, and with the following consequences (that is to say) :—

(1) Preferred and deferred ordinary stock shall be issued only in substitution for equal amounts of paid-up ordinary stock, and by way of division of portions of ordinary stock into two equal parts;

(6) As between preferred ordinary stock and deferred ordinary stock, preferred ordinary stock shall bear a fixed maximum dividend at the rate of six *per centum per annum* ;

(7) In respect of dividend to the extent of the maximum aforesaid, preferred ordinary stock shall at the time of its creation, and at all times afterwards, have priority over deferred ordinary stock created or to be created, and shall rank *parri passu* with the undivided ordinary stock and the ordinary shares of the company created or to be created ; and in respect of dividend, preferred ordinary stock shall at all times and to all intents rank after all preference and guaranteed stock and shares of the company created or to be created ;

(8) In each year after all holders of preferred ordinary stock for the time being issued have received in full the maximum dividend aforesaid, all holders of deferred ordinary stock for the time being issued shall, in respect of all dividend exceeding that maximum paid by the company in that year on ordinary stock and shares, rank *parri passu* with the holders of undivided ordinary stock and of ordinary shares of the company for the time being issued ;

(9) If, nevertheless, in any year ending on the thirty-first day of *December*, there are not profits available for payment to all the holders of preferred ordinary stock of the maximum dividend aforesaid, no part of the deficiency shall be made good out of the profits of any subsequent year, or out of any other funds of the company.

Extension of Scope of Railway Companies Powers Act, 1864.

38.—The Railway Companies Powers Act 1864 shall take effect and apply in the following cases in the same manner as if they were specified in section three of that Act (that is to say):

Where a company desire to make new provisions, or to alter any of the provisions of their special Act, or of the Companies Clauses Consolidation Act 1845, so far as it is incorporated therewith, with respect to all or any of the matters following; namely

(e) The appointment and duties of Auditors.

SCHEDULE I

FORMS OF ACCOUNT PRESCRIBED BY REGULATION OF
RAILWAYS ACT, 1868.

RAILWAY. Half-year ending 18 .

[No. 1.] STATEMENT OF CAPITAL AUTHORISED, AND CREATED BY THE
COMPANY.

ACTS OF PARLIAMENT or Certificates of the Board of Trade.	CAPITAL AUTHORISED			CAPITAL CREATED OR SANCTIONED			BALANCE		
	Stock and Shares	Loans	Total	Stock and Shares	Loans	Total	Stock and Shares	Loans	Total
	£	£	£	£	£	£	£	£	£
1. { [Except where capital powers 2. are comprised in a Consolida- 3. tion Act, each Act or Certificate 4. authorising Capital to be stated 5. here separately in order of &c. date.]									
Total									

[No. 2.] STATEMENT OF STOCK AND SHARE CAPITAL CREATED, SHOWING
THE PROPORTION RECEIVED.

DESCRIPTION	Amount created	Amount received	Calls in arrears	Amount uncalled	Amount unissued
	£	£	£	£	£
[State each class of Stock or Shares in order of date of creation, showing the premium or discount, if any, at which it was issued, the preferential or fixed dividends, if any, to which it is entitled, and any other con- ditions attached to it.]					
Total					

[No. 7.] ESTIMATE OF FURTHER EXPENDITURE OF CAPITAL ACCOUNT.

	FURTHER EXPENDITURE		
	During the Half-year ending	In subsequent Half-years	Total
Lines open for Traffic			
(Particulars showing principal items)			
Lines in course of construction.. ..			
(Details of each line)			
Working Stock			
(Particulars)			
Subscription to other Railways.. ..			
(Specifying Lines)			
Docks, Steamboats, and other special items..			
(Particulars)			
Works not yet commenced and in abeyance (in detail)			
Other items (in detail)			
Total estimated further Expenditure of Capital			

[No. 8.] CAPITAL POWERS AND OTHER ASSETS AVAILABLE TO MEET FURTHER EXPENDITURE, as per No. 7.

Share and Loan Capital authorised or created, but not yet received ..									
Any other Assets (in detail)									
Total									

[No. 9.] *Dr.* REVENUE ACCOUNT. *Cr.*

Half-year ended	EXPENDITURE	£ s d	Half-year ended	RECEIPTS	£ s d £ s d
	To Maintenance of Way, Works and Stations			By Passengers.. ..	
	See Abstract A.			" Parcels, Horses, Carriages, &c. ..	
	" Locomotive Power ..do. B.			" Mails	
	" Carriage and Waggon Repairs .. ..do. C.			" Merchandise ..	
	" Traffic Expenses.. ..do. D.			" Live Stock.. ..	
	" General Charges.. ..do. E.			" Minerals	
	" Law Charges			" Special and Miscellaneous Receipts—	
	" Parliamentary Expenses ..			Such as	
	" Compensation (Accidents and Losses)			Navigation ..	
	" Rates and Taxes.. ..			Steamboats ..	
	" Government Duty			Rents ..	
	" Special and Miscellaneous Expenses (if any)			Transfer Fees, &c.	
	" Balance carried to Net Revenue Account			Details	
		£			£

[No. 10.] *Dr,*

NET REVENUE ACCOUNT.

Cr.

Half-year ended	£ s d	Half-year ended	£ s d
To Interest on Mortgage and Debenture Loans		By Balance brought from last Half-year's Ac- count	
" Interest on Deben- ture Stock		" Ditto Revenue Ac- count, No. 9	
" Interest on Calls in advance		" Dividends on Shares in other Companies ..	
" Interest on Tem- porary Loans		" Bankers and General Interest Account (if in credit)	
" Interest on Lloyd's Bonds		" Special and Miscel- laneous Receipts (if any)	
" Interest on Banking Balances			
" General Interest Account (if in debit)		(Details to be given.)	
" Rents of Leased Lines, Guarantees, &c.			
Details.			
" Special and Miscel- laneous Payments (if any)			
Details.			
" Balance, being Pay- ment available for dividend			
[See No. 13.] £			£

[No. 11.]

PROPOSED APPROPRIATION OF BALANCE AVAILABLE FOR DIVIDEND.

Half-year ended	
	Balance available for Dividend as per Account No. 10 £
	Preference Stock { to be stated in order of creation } £
	Do. { with rate of dividend }
	Do.
	Ordinary Stock (being at the rate of per cent.)
	Balance to next Half-year £

A. MAINTENANCE OF WAY, WORKS, &c.				C. REPAIRS AND RENEWALS OF CARRIAGES AND WAGGONS.			
Half-year ended	£	s	d	Half-year ended	£	s	d
Salaries, Office Expenses and General Superin- tendence				CARRIAGES: Salaries, Office Ex- penses and General Superintendence ..			
Maintenance and Re- newal of Permanent Way				Wages			
Wages				Materials			
Materials				WAGGONS: Salaries, Office Ex- penses and General Superintendence ..			
Repairs of Roads, Bridges, Signals, and Works ..				Wages			
Repairs of Stations and Buildings				Materials			
Special Expenditure (if any)				Total			
MILES MAINTAINED: Double							
Single							
Total							
Total							
B. LOCOMOTIVE POWER.				D. TRAFFIC EXPENSES.			
Half-year ended	£	s	d	Half-year ended	£	s	d
Salaries, Office Expenses and General Superin- tendence				Salaries and Wages, &c. ..			
RUNNING EXPENSES: Wages connected with the working of Loco- motive Engines				Fuel, Lighting, Water, and General Stores			
Coal and Coke				Clothing, Printing, Stationery, and Tickets			
Water				Horses, Harness, Vans, Pro- vender, &c.			
Oil, Tallow, and other Stores				Wagon Covers, Ropes, &c. ..			
REPAIRS AND RENEWALS: Wages				Joint Station Expenses			
Materials				Miscellaneous Expenses			
Special Expenditure ..				Special Expenditure (if any) ..			
£							
E. GENERAL CHARGES.				Half-year ended	£	s	d
				Directors			
				Auditors and Public Account- ants (if any)			
				Salaries of Secretary, General Manager, Accountant, and Clerks			
				Office Expenses			
				Advertising			
				Fire Insurance			
				Electric Telegraph Expenses ..			
				Railway Clearing House Ex- penses			
				Special Expenditure (if any) ..			

[No. 13.] *Dr.*

GENERAL BALANCE SHEET.

Cr.

	£ s d		£ s d
To Capital Account, Balance at credit thereof, as per Account No. 4		By Cash at Bankers—Current Account	
" Net Revenue Account, Balance at credit thereof, as per Account No. 10		" Cash on Deposit at Interest	
" Unpaid Dividends and Interest		" Cash Invested in Consols and Government Securities	
" Guaranteed Dividends and Interest payable or accruing and provided for		" Cash Invested in Shares of other Railway Companies not charged as Capital Expenditure	
" Temporary Loans		" General Stores—Stock of Materials on hand	
" Lloyd's Bond and other obligations not included in Loan Capital Statement, No. 3		" Traffic Accounts Due to the Company	
" Balance Due to Bankers		" Accounts Due by other Companies	
" Debts Due to other Companies		" Do. Clearing House	
" Amount Due to Clearing House		" Do. Post Office	
" Sundry Outstanding Accounts		" Sundry Outstanding Accounts	
" Fire Insurance Fund on Stations, Works, and Buildings		" Suspense Accounts (if any)	
" Insurance Fund on Steamboats		<i>To be enumerated.</i>	
" Special Items		" Special Items	
	£		£

[No. 14.]

MILEAGE STATEMENT.

Half-year ended		Miles Authorised	Miles Constructed	Miles Constructed or to be Constructed	Miles Worked by Engines
	Lines Owned by Company				
	Lines Partly Owned				
	Lines Leased or Rented				
	Total				
	Lines Worked				
	Foreign Lines Worked Over				
	Total				

[No. 15.]

STATEMENT OF TRAIN MILEAGE.

Half-year ended					
	Passenger Trains				
	Goods and Mineral Trains				
	Total				

(Signed)

Chairman or Deputy-Chairman of Company.
Secretary or Accountant of Company.

CERTIFICATE RESPECTING THE PERMANENT WAY, &c.

I hereby certify that the whole of the Company's Permanent Way, Stations, Buildings, Canals, and other Works have during the past half-year been maintained in good working condition and repair.

Date 18 . Engineer.

CERTIFICATE RESPECTING THE ROLLING STOCK.

I hereby certify that the whole of the Company's Plant, Engines, Tenders, Carriages, Wagons, Machinery, and Tools, also the Marine Engines of the Steam Vessels, have during the past half-year been maintained in good working order and repair.

Date 18 . { Chief Engineer or
Locomotive Superintendent.

AUDITOR'S CERTIFICATE.

(As prescribed by Act 30 and 31 Victoria, cap. 127, sec. 30.)

THE REGULATION OF RAILWAYS ACT, 1889.

52 and 53 Vict. c. 57.

Capital and Revenue Expenditure.

3.—Whenever any railway company shall be ordered by the Board of Trade to provide any appliances, or execute any works or incur any expenditure, under the provisions of this Act, which would properly be chargeable to Capital Account, it shall be lawful for such company to furnish to the Board of Trade an estimate of the cost of providing such appliances, executing such works, and carrying out such order generally, and thereupon the Board of Trade shall, upon the application of the company, fix and determine the amount which would properly be capital expenditure, and the company may from time to time issue debentures or debenture stock in priority to or ranking *pari passu* with any existing debentures or debenture stock of such company bearing interest at a rate not exceeding five per cent. per annum to an amount not exceeding the sum so paid and determined, and any money raised under the provision of this section shall be applied in carrying out such requirements of the Board of Trade, and to no other purpose whatsoever, and no other authority save the certificate of the Board of Trade shall be requisite to authorise and validate the issue of such debentures or debenture stock.

PARTNERSHIPS.

THE PARTNERSHIP ACT, 1890.

53 and 54 Vict. c. 39.

21.—Unless the contrary intention appears, property bought with money belonging to the firm is deemed to have been bought on account of the firm.

24.—The interests of partners in the partnership property, and their rights and duties in relation to the partnership, shall be determined subject to any agreement, express or implied, between the partners by the following rules:—

- (1) All the partners are entitled to share equally in the capital and profits of the business, and must contribute equally towards the losses, whether of capital or otherwise, sustained by the firm.
- (2) The firm must indemnify every partner in respect of payments made and personal liabilities incurred by him
 - (a) In the ordinary and proper conduct of the business of the firm; or,
 - (b) In or about anything necessarily done for the preservation of the business or property of the firm.
- (3) A partner making, for the purpose of the partnership, any actual payment or advance beyond the amount of capital which he has agreed to subscribe, is entitled to interest at the rate of five per cent. per annum from the date of the payment or advance.
- (4) A partner is not entitled, before the ascertainment of profits, to interest on the capital subscribed by him.
- (5) Every partner may take part in the management of the partnership business.
- (6) No partner shall be entitled to remuneration for acting in the partnership business.
- (7) No person may be introduced as a partner without the consent of all existing partners.
- (8) Any difference arising as to ordinary matters connected with the partnership business may be decided by a majority of the partners, but no change may be made in the nature of the partnership business without the consent of all existing partners.

- (9) The partnership books are to be kept at the place of business of the partnership (or the principal place, if there is more than one), and every partner may, when he thinks fit, have access to and inspect and copy any of them.

28.—Partners are bound to render true accounts and full information of all things affecting the partnership to any partner or his legal representatives.

29.—(1) Every partner must account to the firm for any benefit derived by him without the consent of the other partners from any transaction concerning the partnership, or from any use by him of the partnership property, name, or business connection.

(2) This section applies also to transactions undertaken after a partnership has been dissolved by the death of a partner, and before the affairs thereof have been completely wound up, either by any surviving partner or by the representatives of the deceased partner.

39.—On the dissolution of a partnership, every partner is entitled, as against the other partners in the firm, and all persons claiming through them in respect of their interests as partners, to have the property of the partnership applied in payment of the debts and liabilities of the firm, and to have the surplus assets, after such payment, applied in payment of what may be due to the partners respectively, after deducting what may be due from them as partners to the firm; and for that purpose any partner or his representatives may, on the termination of the partnership, apply to the Court to wind up the business and affairs of the firm.

40.—Where one partner has paid a premium to another on entering into a partnership for a fixed term, and the partnership is dissolved before the expiration of that term otherwise than by the death of a partner, the Court may order the repayment of the premium, or of such part thereof as it thinks just, having regard to the terms of the partnership contract, and to the length of time during which the partnership has continued: unless—

- (a) the dissolution is, in the judgment of the Court, wholly or chiefly due to the misconduct of the partner who paid the premium; or,
(b) the partnership has been dissolved by an agreement containing no provision for a return of any part of the premium.

42.—(1) Where any member of a firm has died, or otherwise ceased to be a partner, and the surviving or continuing partners carry on the business of the firm, with its capital or assets, without any final settle-

ment of accounts as between the firm and the outgoing partner or his estate, then, in the absence of any agreement to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since the dissolution as the Court may find to be attributable to the use of his share of the partnership assets, or to interest at the rate of five per centum per annum on the amount of his share of the partnership assets.

(2) Provided that where by the partnership contract an option is given to surviving or continuing partners to purchase the interest of the deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner, or the outgoing partner, or his estate, as the case may be, is not entitled to any further or other share of profits: but if any partner, assuming to act in exercise of the option, does not in all material respects comply with the terms thereof, he is liable to account under the foregoing provisions of this section.

43.—Subject to any agreement between the partners, the amount due from surviving or continuing partners to an outgoing partner, or the representative of a deceased partner, in respect of the outgoing or deceased partner's share, is a debt accruing at the date of the dissolution or death.

44.—In settling accounts between the partners after dissolution of partnership, the following rules shall, subject to any agreement, be observed:—

- (a) Losses, including losses and deficiencies of capital, shall be paid first out of profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits:
- (b) The assets of the firm, including the sums, if any, contributed by the partners to make up losses or deficiencies of capital, shall be applied in the following manner and order:—
 - (1) In paying the debts and liabilities of the firm to persons who are not partners therein:
 - (2) In paying to each partner rateably what is due from the firm to him for advances as distinguished from capital:
 - (3) In paying to each partner rateably what is due from the firm to him in respect of capital:
 - (4) The ultimate residue, if any, shall be divided among the partners in the proportion in which profits are divisible.

LICENSED PROPERTY.

THE LICENSING ACT, 1904.

4 Edw. VII. c. 23.

1.—(1) The power to refuse the renewal of an existing on-licence, on any ground other than the ground that the licensed premises have been ill-conducted or are structurally deficient, or structurally unsuitable, or grounds connected with the character or fitness of the proposed holder of the licence or the ground that the renewal would be void, shall be vested in Quarter Sessions instead of the Justices of the Licensing District, but shall only be exercised on a reference from those justices, and on payment of compensation in accordance with this Act.

(2) In every case of the refusal of the renewal of an existing on-licence by the Justices of a Licensing District, they shall specify in writing to the applicant the grounds of their refusal.

2.—(1) Where Quarter Sessions refuse the renewal of an existing on-licence under this Act, a sum equal to the difference between the value of the licensed premises (calculated as if the licence were subject to the same conditions of renewal as were applicable immediately before the passing of this Act, and including in that value the amount of any depreciation of trade fixtures arising by reason of the refusal to renew the licence) and the value which those premises would bear if they were not licensed premises shall be paid as compensation to the persons interested in the licensed premises.

(2) The amount to be so paid shall, if an amount is agreed upon by the persons appearing to Quarter Sessions to be interested in the licensed premises, and is approved by Quarter Sessions, be that amount, and in default of such agreement and approval shall be determined by the Commissioners of Inland Revenue in the same manner and subject to the like appeal to the High Court as on the valuation of an estate for the purpose of estate duty, and in any event the amount shall be divided amongst the persons interested in the licensed premises (including the holder of the licence) in such shares as may be determined by Quarter Sessions :

Provided that, in the case of the licence-holder, regard shall be had not only to his legal interest in the premises or trade fixtures, but also to his conduct and to the length of time during which he has been the holder of the licence, and the holder of a licence, if a tenant, shall (notwithstanding any agreement to the contrary) in no case receive a less amount than he would be entitled to as tenant from year to year of the licensed premises.

(4) Any costs incurred by the Commissioners of Inland Revenue on an appeal from their decision to the High Court under this section shall, unless the High Court order those costs to be paid by some party to the appeal other than the Commissioners, be paid out of the amount to be paid as compensation.

3.—(1) Quarter Sessions shall, in each year, unless they certify to the Secretary of State that it is unnecessary to do so in any year, for the purposes of this Act impose, in respect of all existing on-licences renewed in respect of premises within their area, charges at rates not exceeding and graduated in the same proportion as the rates shown in the scale of maximum charges set out in the First Schedule to this Act.

(2) Charges payable under this section in respect of any licence shall be levied and paid together with and as part of the duties on the corresponding excise licence, but a separate account shall be kept by the Commissioners of Inland Revenue of the amount produced by those charges in the area of any Quarter Sessions, and that amount shall in each year be paid over to that Quarter Sessions in accordance with rules made by the Treasury for the purpose.

(3) Such deductions from rent as are set out in the Second Schedule to this Act may, notwithstanding any agreement to the contrary, be made by any licence-holder who pays a charge under this section, and also by any person from whose rent a deduction is made in respect of the payment of such a charge.

(4) Any sums paid under this Act to Quarter Sessions in respect of the charges under this section, or received by Quarter Sessions from any other source for the payment of compensation under this Act, shall be paid by them to a separate account under their management, and the moneys standing to the credit of that account shall constitute the Compensation Fund.

(5) Any expenses incurred by Quarter Sessions in the payment of compensation under this Act, or otherwise in the exercise of their powers or the performance of their duties under this Act, and such expenses of the Justices of the Licensing District incurred under this Act as Quarter Sessions may allow, shall be paid out of the Compensation Fund, and Quarter Sessions, in the exercise of their powers under this Act, shall have regard to the funds available for the purpose.

Quarter Sessions may, with the consent of a Secretary of State, borrow, in accordance with rules made under this Act on the security of the Compensation Fund, for the purpose of paying any compensation payable under this Act.

6.—A Secretary of State may make rules for carrying into effect this Act, and may by those rules, amongst other things:—

- (b) Provide for the enforcement of any security given for money borrowed, and for the time, not exceeding fifteen years, within which money borrowed is to be replaced; and
- (c) regulate the management and application of the Compensation Fund, and the audit of the Accounts of Quarter Sessions.

SCHEDULE I.

Scale of Maximum Charges.

Section 3.

Annual Value of Premises to be taken as for the purpose of the Publican's Licence Duty.

Maximum Rate of Charge.

£	£					£	s	d
	Under 15	..	..	..	..	1	0	0
15	and under 20	..	..	..	..	2	0	0
20	„ 25	..	..	..	..	3	0	0
25	„ 30	..	..	..	..	4	0	0
30	„ 40	..	..	..	..	6	0	0
40	„ 50	..	..	..	..	10	0	0
50	„ 100	..	..	..	..	15	0	0
100	„ 200	..	..	..	..	20	0	0
200	„ 300	..	..	..	..	30	0	0
300	„ 400	..	..	..	..	40	0	0
400	„ 500	..	..	..	..	50	0	0
500	„ 600	..	..	..	..	60	0	0
600	„ 700	..	..	..	..	70	6	0
700	„ 800	..	..	..	..	80	0	0
800	„ 900	..	..	..	..	90	0	0
900	and over.	..	..	..	..	100	0	0

SCHEDULE II.

Scale of Deductions.

Section 3.

A person whose unexpired term does not exceed—

1 year, may deduct a sum equal to 100 per cent of the charge.

2 years	„	88	„
3	„	82	„
4	„	76	„
5	„	70	„
6	„	65	„
7	„	60	„
8	„	55	„
9	„	50	„
10	„	45	„
11	„	41	„

A person whose unexpired terms does not exceed—

12 years, may deduct a sum equal to 37 per cent. of the charge.

13	„	„	33	„
14	„	„	29	„
15	„	„	25	„
16	„	„	23	„
17	„	„	21	„
18	„	„	19	„
19	„	„	17	„
20	„	„	15	„
21	„	„	14	„
22	„	„	13	„
23	„	„	12	„
24	„	„	11	„
25	„	„	10	„

Exceeds 25, but does not exceed 30, years may deduct a sum equal to 7 per cent. of the charge.

Exceeds 30, but does not exceed 35, years may deduct a sum equal to 6 per cent. of the charge.

Exceeds 35, but does not exceed 40, years may deduct a sum equal to 5 per cent. of the charge.

Exceeds 40, but does not exceed 45, years may deduct a sum equal to 4 per cent. of the charge.

Exceeds 45, but does not exceed 50, years may deduct a sum equal to 3 per cent. of the charge.

Exceeds 50, but does not exceed 55, years may deduct a sum equal to 2 per cent. of the charge.

Exceeds 55, but does not exceed 60, years may deduct a sum equal to 1 per cent. of the charge.

But the amount deducted shall in no case exceed half the rent.

THE LICENSING RULES 1904.

Rules made by the Secretary of State for the Home Department, dated December 20th 1904, under Section 6 of the Licensing Act, 1904:—

Accounts.

61.—(1) It shall be the duty of the Compensation Authority to cause proper accounts to be kept in connection with the Compensation Fund, and a Financial Statement to be prepared at the close of each year in the form directed by the Secretary of State.

(2) The accounts shall be made up for each calendar year, or for such other period as the Compensation Authority, with the approval of the Secretary of State, determine.

Audit by Professional Accountant.

62.—(1) The Compensation Authority shall appoint a professional accountant, approved by the Secretary of State, to be the Auditor of their accounts.

(2) The Auditor may be appointed for a term not exceeding three years, but a retiring Auditor shall be eligible for reappointment.

(3) The remuneration of the Auditor shall be such as may be fixed by the Compensation Authority, with the consent of a Secretary of State.

Examination of Accounts.

63.—As soon as may be after close of the year for which the accounts are made up the Compensation Authority shall submit to the Auditor for examination the detailed accounts, together with the vouchers and authorities for receipts and payments, and shall also submit, for the Auditor's certificate, the Annual Financial Statement required by these rules.

64.—A copy of the Financial Statement, as certified by the Auditor, shall be sent by the Compensation Authority to the Secretary of State, together with a copy of any report made by the auditor in regard thereto.

CORPORATION ACCOUNTS.

THE PUBLIC HEALTH ACT, 1875.

38 and 39 Vict. c. 55.

Officers entrusted with Money to give Security.

194.—Before any officer or servant of a local authority enters on any office or employment under this Act by reason whereof he will or may be entrusted with the custody or control of money, the local authority by whom he is appointed shall take from him sufficient security for the faithful execution of such office or employment, and for duly accounting for all moneys which may be entrusted to him by reason thereof.

Officers to Account.

195.—Every officer and servant appointed or employed under this Act by a local authority shall, when and in such manner as may be required by such authority, make out and deliver to them a true and perfect account in writing of all moneys received by him for the purposes of this Act, stating how, and to whom, and for what purpose such moneys have been disposed of, and shall, together with such account, deliver

the vouchers or receipts for all payments made by him, and pay over to the treasurer all moneys owing by him on the balance of accounts.

And every such officer or servant employed in the collection of any rate made under this Act shall, within seven days after he has received any moneys on account of any such rate, pay over the same to the treasurer, and shall, as and when the local authority may direct, deliver a list signed by him and containing the names of all persons who have neglected or refused to pay any such rate, and the sums respectively due from them.

Summary of Proceedings against Defaulting Officers.

196.—If any officer or servant appointed or employed under this Act by a local authority—

Fails to render accounts, or to produce and deliver up vouchers and receipts, or to pay over any moneys, as and when required by this Act, or

Fails within five days after written notice in that behalf from the local authority to deliver up to the local authority all books, papers, writings, property and things, in his possession or power, relating to the execution of this Act, or belonging to such authority, the local authority may complain to any justice, and such justice shall thereupon summon the party charged to appear before a Court of summary jurisdiction.

On the appearance of the party charged, or on proof that the summons was personally served on him, or left at his last known place of abode or business, if it appears to the Court that he has failed to render any such accounts, or to pay over such moneys, or to produce and deliver up any such vouchers or receipts, books, papers, writings, property, or things, as aforesaid, in accordance with the provisions of this Act, and that he still fails or refuses so to do, the Court may commit the offender to gaol, there to remain without bail until he has rendered such accounts, paid over such moneys, and produced and delivered up all such vouchers, receipts, books, papers, writings, property and things in respect of which the charge was made: Provided that a person shall not be imprisoned under this section for a period exceeding six months.

No proceeding under this section shall be construed to relieve or discharge any surety of the offender from any liability whatever.

Mode of Defraying Expenses of Urban Authority.

207.—All expenses incurred or payable by an urban authority in the execution of this Act, and not otherwise provided for, shall be charged

on and defrayed out of the district fund and general district rate leviable by them under this Act, subject to the following exceptions, namely:—

That, if in any district the expenses incurred by an urban authority (being the council of a borough) in the execution of the Sanitary Acts were, at the time of the passing of this Act, payable out of the borough fund or borough rate, then the expenses incurred by that authority in the execution of this Act shall be charged on and defrayed out of the borough fund or borough rate; and

That, if in any district the expenses incurred by an urban authority (being improvement commissioners) in the execution of the Sanitary Acts were, at the time of the passing of this Act, payable out of any rate in the nature of a general district rate leviable by them as such commissioners throughout the whole of their district, then the expenses incurred by that authority in the execution of this Act shall be charged on and defrayed out of such rate; and for the purposes of this section the council of the borough of Folkestone shall be deemed to be improvement commissioners; and

That where at the time of the passing of this Act expenses incurred by an urban authority in the execution of certain purposes of the Sanitary Acts were payable out of the borough fund and borough rate, and the expenses incurred by such authority in the execution of the other purposes of the said Acts were payable out of a rate or rates leviable by that authority throughout the whole of their district for paving, sewerage, and other sanitary purposes, then the expenses incurred by that authority in the execution of the same or similar purposes respectively under this Act shall respectively be charged on and defrayed out of the borough fund and borough rate, and out of the rate or rates leviable as aforesaid.

Power in certain cases by Provisional Order to alter Mode.

208.—Where at the time of the passing of this Act the expenses incurred by an urban authority for sanitary purposes are payable otherwise than in the manner provided by the Local Government Acts, the Local Government Board may, on the application of such authority, or of any ten persons rated to the relief of the poor within the district, declare by provisional order that the expenses of such authority incurred in the execution of this Act shall be defrayed out of a district fund and general district rate to be levied by them under this Act, subject to the provisions of this Act with respect to the mode of defraying in certain cases the expenses of the repair of highways.

District Fund Account.

209.—In the district of every urban authority whose expenses under this Act are directed to be defrayed out of the district fund and general

district rate there shall be continued or established a fund called "the district fund": a separate account called "the District Fund Account" of all moneys carried under this Act to the account of that fund shall be kept by the treasurer of the urban authority; and such moneys shall be applied by the urban authority in defraying such of the expenses chargeable thereon under this Act as they may think proper.

Making General District Rate.

210.—For the purpose of defraying any expenses chargeable on the district fund which that fund is insufficient to meet, the urban authority shall from time to time, as occasion may require, make by writing under their common seal, and levy in addition to any other rate leviable by them under this Act, a rate or rates to be called "general district rates."

Any such rate may be made and levied either prospectively in order to raise money for the payment of future charges and expenses, or retrospectively in order to raise money for the payment of charges and expenses incurred at any time within six months before the making of the rate: in calculating the period of six months during which the rate may be made retrospectively, the time during which any appeal or other proceeding relating to such rate is pending shall be excluded.

Public notice of intention to make any such rate, and of the time when it is intended to make the same, and of the place where a statement of the proposed rate is deposited for inspection shall be given by the urban authority in the week immediately before the day on which the rate is intended to be made, and at least seven days previously thereto; but in case of proceedings to levy or recover any rate it shall not be necessary to prove that such notice was given.

BORROWING POWERS.

Power to Borrow on Credit of Rates.

233.—Any local authority may, with the sanction of the Local Government Board, for the purpose of defraying any costs, charges, and expenses incurred or to be incurred by them in the execution of the Sanitary Acts, or of this Act, or for the purpose of discharging any loans contracted under the Sanitary Acts or this Act, borrow or re-borrow, and take up at interest, any sums of money necessary for defraying any such costs, charges, and expenses, or for discharging any such loans as aforesaid.

An urban authority may borrow or re-borrow any such sums on the credit of any fund or all or any rates or rate out of which they are authorised to defray expenses incurred by them in the execution of this Act, and for the purpose of securing the repayment of any sums so

borrowed, with interest thereon, they may mortgage to the persons by or on behalf of whom such sums are advanced any such fund or rates or rate.

A rural authority may borrow or re-borrow any such sums, if applied or intended to be applied to general expenses of such authority, on the credit of the common fund out of which such expenses are payable, and if applied or intended to be applied to special expenses of such authority, on the credit of any rate or rates out of which such expenses are payable, and for the purpose of securing the repayment of any sums so borrowed, with interest thereon, they may mortgage to the persons by or on behalf of whom such sums are advanced any such fund, rate, or rates.

Regulations as to exercise of Borrowing Powers.

234.—The exercise of the powers of borrowing conferred by this Act shall be subject to the following regulations; (namely)

- (1) Money shall not be borrowed except for permanent works (including under this expression any works of which the cost ought in the opinion of the Local Government Board to be spread over a term of years):
- (2) The sum borrowed shall not at any time exceed, with the balances of all the outstanding loans contracted by the local authority under the Sanitary Acts and this Act, in the whole, the assessable value for two years of the premises assessable within the district in respect of which such money may be borrowed:
- (3) Where the sum proposed to be borrowed with such balances (if any) would exceed the assessable value for one year of such premises, the Local Government Board shall not give their sanction to such loan until one of their inspectors has held a local inquiry and reported to the said Board:
- (4) The money may be borrowed for such time, not exceeding sixty years, as the local authority, with the sanction of the Local Government Board, determine in each case; and, subject as aforesaid, the local authority shall either pay off the moneys so borrowed by equal annual instalments of principal, or of principal and interest, or they shall in every year set apart as a sinking fund, and accumulate in the way of compound interest by investing the same in the purchase of Exchequer Bills or other Government securities such sum as will with accumulations in the way of compound interest be sufficient, after payment of all expenses, to pay off the moneys so borrowed within the period sanctioned:

- (5) A local authority may at any time apply the whole or any part of a sinking fund set apart under this Act in or towards the discharge of the moneys for the repayment of which the fund has been established : Provided that they pay into the fund in each year and accumulate until the whole of the moneys borrowed are discharged a sum equivalent to the interest which would have been produced by the sinking fund or the part of the sinking fund so applied :
- (6) Where money is borrowed for the purpose of discharging a previous loan the time for repayment of the money so borrowed shall not extend beyond the unexpired portion of the period for which the original loan was sanctioned, unless with the sanction of the Local Government Board, and shall in no case be extended beyond the period of sixty years from the date of the original loan.

Where any urban authority borrow any money for the purpose of defraying private improvement expenses, or expenses in respect of which they have determined a part only of the district to be liable, it shall be the duty of such authority, as between the ratepayers of the district, to make good, as far as they can, the money so borrowed, as occasion requires, either out of private improvement rates, or out of a rate levied in such part of the district as aforesaid.

Power to Borrow on Credit of Sewage and Land Plant.

235.—Where any local authority are possessed of any lands, works, or other property for the purposes of disposal of sewage pursuant to this Act, they may borrow any moneys on the credit of such lands, works, or other property, and may mortgage such lands, works, or other property to any person advancing such moneys, in the same manner in all respects as if they were the absolute owner, both at law and in equity, of the lands, works, or other property so mortgaged. The moneys so borrowed shall be applied for purposes for which moneys may be borrowed under this Act, but it shall not be in any way incumbent on the mortgagees to see to the application of such moneys, nor shall they be responsible for any misapplication thereof.

The powers of borrowing conferred by this section shall, where the sums borrowed do not exceed three-fourths of the purchase-money of such lands (but not otherwise), be deemed to be distinct from, and in addition to, the general borrowing powers conferred on a local authority by this Act. Any local authority may pay out of any rates leviable by them for purposes of this Act the interest on any moneys borrowed by such authority in pursuance of this section.

Audit where Urban Authority are a Town Council.

246.—Where an urban authority are the council of the borough the accounts of the receipts and expenditure under this Act of such authority

shall be audited and examined by the Auditors of the borough, and shall be published in like manner, and at the same time, as the municipal accounts, and the Auditors shall proceed in the audit after like notice and in like manner, shall have like powers and authorities, and perform like duties, as in the case of auditing the municipal accounts.

Each of such Auditors shall in respect of each audit be paid such reasonable remuneration, not being less than two guineas for every day in which they are employed in such audit, as such authority from time to time appoint. Any order of such authority for the payment of any money may be moved by *certiorari*, and like proceedings may be had thereon as under section forty-four of the Act of the first year of Her Majesty, chapter seventy-eight, with respect to orders of the council of a borough for payments out of the borough fund.

Audit where Urban Authority are not a Town Council.

247.—Where an urban authority are not the council of a borough the following regulations with respect to audit shall be observed; (namely)

- (1) The accounts of the receipts and expenditure under this Act of such authority shall be audited and examined once in every year as soon as can be after the twenty-fifth day of March, by the Auditor of accounts relating to the relief of the poor for the union in which the district of such authority, or the greater part thereof, is situate, unless such Auditor is a member of the authority whose accounts he is appointed to audit, in which case such accounts shall be audited by such Auditor of any adjoining union as may from time to time be appointed by the Local Government Board :
- (2) There shall be paid to such Auditor in respect of each audit under this Act such reasonable remuneration, not being less than two guineas for every day in which he is employed in such audit, as such authority from time to time appoint, together with his expenses of travelling to and from the place of audit :
- (3) Before each audit such authority shall, after receiving from the Auditor the requisite appointment, give at least fourteen days' notice of the time and place at which the same will be made, and of the deposit of accounts required by this section, by advertisement in some one or more of the local newspapers circulated in the district ; and the production of the newspaper containing such notice shall be deemed to be sufficient proof of such notice on any proceeding whatsoever :
- (4) A copy of the accounts, duly made up and balanced, together with all rate books, account books, deeds, contracts, accounts, vouchers,

and receipts mentioned or referred to in such accounts, shall be deposited in the office of such authority, and be open during office hours thereat, to the inspection of all persons interested for seven clear days before the audit, and all such persons shall be at liberty to take copies of, or extracts from, the same without fee or reward; and any officer of such authority duly appointed in that behalf neglecting to make up such accounts and books, or altering such accounts and books, or allowing them to be altered when so made up, or refusing to allow inspection thereof, shall be liable to a penalty not exceeding five pounds :

- (5) For the purpose of any audit under this Act, every Auditor may, by summons in writing, require the production before him of all books, deeds, contracts, accounts, vouchers, receipts, and other documents and papers which he may deem necessary, and may require any person holding or accountable for any such books, deeds, contracts, accounts, vouchers, receipts, documents, or papers to appear before him at any such audit or any adjournment thereof, and to make and sign a declaration as to the correctness of the same; and if any such person neglects or refuses so to do, or to produce any such books, deeds, contracts, accounts, vouchers, receipts, documents, or papers, or to make or sign such declaration, he shall incur for every neglect or refusal a penalty not exceeding forty shillings; and if he falsely or corruptly makes or signs any such declaration, knowing the same to be untrue in any material particular, he shall be liable to the penalties inflicted on persons guilty of wilful and corrupt perjury :
- (6) Any ratepayer or owner of property in the district may be present at the audit, and may make any objection to such accounts before the Auditor; and such ratepayers and owners shall have the same right of appeal against allowances by an Auditor as they have by law against disallowances :
- (7) Any Auditor acting in pursuance of this section shall disallow every item of account contrary to law, and surcharge the same on the person making or authorising the making of the illegal payment, and shall charge against any person accounting the amount of any deficiency or loss incurred by the negligence or misconduct of that person, or of any sum which ought to have been, but is not, brought into account by that person, and shall in every such case certify the amount due from such person, and on application by any party aggrieved shall state in writing the reasons for his decision in respect of such disallowance or surcharge, and also of any allowance which he may have made :

- (8) Any person aggrieved by disallowance made may apply to the Court of Queen's Bench for a writ of *certiorari* to remove the disallowance into the said Court, in the same manner and subject to the same conditions as are provided in the case of disallowances by Auditors under the laws for the time being in force with regard to the relief of the poor ; and the said Court shall have the same powers with respect to allowances, disallowances, and surcharges under this Act as it has with respect to disallowances or allowances by the said Auditors ; or in lieu of such application any person so aggrieved may appeal to the Local Government Board, which Board shall have the same powers in the case of the appeal as it possesses in the case of appeals against allowances, disallowances, and surcharges by the said Poor Law Auditors :
- (9) Every sum certified to be due from any person by an Auditor under this Act shall be paid by such person to the treasurer of such authority within fourteen days after the same has been so certified, unless there is an appeal against the decision ; and if such sum is not so paid, and there is no such appeal, the Auditor shall recover the same from the person against whom the same has been certified to be due by the like process, and with the like powers, as in the case of sums certified on the audit of the poor rate accounts, and shall be paid by such authority all such costs and expenses, including a reasonable compensation for loss of time incurred by him in such proceedings, as are not recovered by him from such person :
- (10) Within fourteen days after the completion of the audit, the Auditor shall report on the accounts audited and examined, and shall deliver such report to the clerk of such authority, who shall cause the same to be deposited in their office, and shall publish an abstract of such accounts in some one or more of the local newspapers circulated in the district.

Where the provisions as to audit of any local Act constituting a board of improvement commissioners are repugnant to, or inconsistent with, those of this Act, the audit of the accounts of such improvement commissioners shall be conducted in all respects in accordance with the provisions of this Act.

FORM (O).—FINANCIAL STATEMENT—*continued.*

EXPENDITURE OTHER THAN FROM LOANS.

	Amount	Totals
	£ s d	£ s d
PUBLIC WORKS.		
Sewerage		
Water Supply		
Gas Supply		
Highways (less amount* borne by County Authority in respect of Repairs of Main Roads, if any)		
Scavenging and Watering		
Parks or Public Pleasure Grounds		
Hospitals		
Other Public Works		
	£ s d	
*Amount borne by County Authority		
PRIVATE IMPROVEMENT WORKS.		
Drainage and Water Supply		
Other Private Improvement Works		
Amount of Expenditure on Public Works and Private Improvement Works		
GENERAL EXPENDITURE.		
Election Expenses		
Legal Expenses		
Salaries (less amount † borne by Parliamentary Grant), viz.:		
Clerk		
Treasurer		
Medical Officer of Health		
Inspector of Nuisances		
Surveyor		
Establishment Charges, other than Salaries		
Repayment of Loans, with Interest ‡		
Expenses of School Attendance Committee (if any)		
Other Payments (excluding contributions on Precepts of Joint Boards or Port Sanitary Authorities)†		
‡Amount borne by Parliamentary Grant:	£ s d	
Medical Officer of Health		
Inspector of Nuisances		
‡Amount paid on Precepts:	£ s d	
To Joint Boards		
To Port Sanitary Authorities		
BURIAL BOARD EXPENDITURE.		
Amount of Expenditure by the Local Board as a Burial Board, where acting in the latter capacity**		
Total Expenditure included in this Statement		

† The particulars required with respect to Loans are to be supplied in the Form (Q) annexed.

** The amount to be inserted here will be the total expenditure shown in the Form (P) annexed.

_____ Clerk [or _____] to the Local Board.
_____ day of _____ 188 .

I hereby certify that I have compared the entries in the above Statement with the Vouchers and other documents relating thereto, and that the regulations with respect to such Statement have been duly complied with.

I hereby further certify that I have ascertained by Audit the correctness of such Statement, and that the amount expended by the Local Board during the year ended the 25th day of March 188 , as included in such Statement and allowed by me at the Audit, is [here insert the amount in words at length].

As witness my hand this _____ day of _____ 188 .

Stamp

District Auditor.

FORM (P).
T (BURIAL BOARD).

LOCAL GOVERNMENT DISTRICT (BURIAL BOARD).

STATEMENT of Receipts and Expenditure by the Local Board for the above-named Local Government District, acting as the Burial Board for that District [or for the of comprised in that District], for the Year ended the 25th day of March 188 .

RECEIPTS OTHER THAN FROM LOANS.

EXPENDITURE OTHER THAN FROM LOANS.

	Totals	Amounts	Totals
	£ s d	£ s d	£ s d
From Poor Rate		
" Burial Board Rate or General District Rate		
" Burial Fees		
Expenses in respect of Burial Grounds and Buildings Clerk Superintendent of Cemetery Salaries, viz.:— { Keeper of Cemetery			
Establishment Charges, other than Salaries			
Repayment of Loans, with Interest*			
Burial Fees paid to Ministers and Incumbents			
Other Payments:—			
Total Expenditure included in this Statement .. £			
Gross Receipts .. £			

* The particulars required with respect to Loans are to be supplied in the "Loan Account" (Form Q) annexed.

Clerk [or _____] to the Burial Board,
_____ day of _____, 188_____

Examined by me in connection with the Financial Statement for the Year ended the 25th day of March 188 , and found correct.

_____ day of _____ 188 _____
District Auditor.

FORM (Q).—LOAN ACCOUNT

.....LOCAL GOVERNMENT DISTRICT.

STATEMENT with reference to Loans obtained by the Local Board for the above-named District
[otherwise than as a Burial Board].*Year ended the *Twenty-fifth day of March* 188 .

Amount originally Advanced	When Advanced	Whether by Public Works Loan Commis- sioners, a Company,† or otherwise	For what Object‡	For what Period	Rate of Interest	Mode of Repay- ment, whether by Annuity or otherwise.	Amounts Paid this Year		Amount of Principal still Owing	Amount annually set apart Interest on which Fund is based	Total Sum in Fund	Securities in which Fund is invested, and Rate of Interest Payable on them
							Principal	Interest				
£							£	£	£	£	£	

* Where the Local Board do not act as a Burial Board the second of these tabular statements [see next page] is to be omitted, as well as the words within brackets at the head of the first of the statements [above].

† If by a Company, insert the name.

‡ Where all or any portion of the Loan has been expended during the year, state the nature of the works and the amount expended in each case.

Nature of Works	Amount Expended
	£

FORM (Q).—LOAN ACCOUNT—continued.

.....LOCAL GOVERNMENT DISTRICT.

* STATEMENT with reference to Loans obtained by the Local Board for the above-named District, acting as the Burial Board.

Year ended the Twenty-fifth day of March 188 .

Amount originally Advanced.	When Advanced.	Whether by Public Works Loan Commis- sioners, a Company,† or otherwise.	For what Object †	For what Period	Rate of Interest	Mode of Repay- ment, whether by Annuity or otherwise	Amounts paid this Year		Principal still owing	SINKING FUND.			
							Principal	Interest		Amount annually set apart	Rate of Interest on which Fund is based	Total Sum in Fund	Securities in which Fund is invested and Rate of Interest Payable on them
£							£	£	£	£		£	

* Where the Local Board do not act as a Burial Board the second of the above tabular statements is to be omitted, as well as the words within brackets at the head of the first of those statements.

† If by a Company, insert the name

‡ Where all or any portion of the Loan has been expended during the year, state the nature of the works and the amount expended in each case.

Clerk to the Local Board,

day of 188 .

Examined by me in connection with the Financial Statement for the year ended the 25th day of March 188 , and found correct.

Nature of Works.

Amount
Expended
£

District Auditor,

day of 188 .

NOTE.—It is only required that money be entered in the Form above to the nearest £; whenever the fractional parts, in abstracting from the Books, amount in their total to 10s. or more than 10s. they are to be taken as equal to £1; if less than 10s. they are to be rejected. Thus, £175 10s. should be entered as £176, but £175 9s. 11d. as £175 only.

THE MUNICIPAL CORPORATIONS ACT, 1882.

*45 and 46 Vict c. 50.**The Treasurer.*

18.—(1) The council shall from time to time appoint a fit person, not a member of the council, to be the treasurer of the borough.

(2) The treasurer shall hold office during the pleasure of the council.

(3) A vacancy in the office shall be filled within twenty-one days after its occurrence.

(4) The offices of town clerk and treasurer shall not be held by the same person.

Other Borough Officers.

19.—The council shall from time to time appoint such other officers as have been usually appointed in the borough, or as the council think necessary, and may at any time discontinue the appointment of any officer appearing to them not necessary to be reappointed.

Security by, and Remuneration of, Officers.

20.—The council shall require every officer appointed by them to give such security as they think proper for the due execution of his office, and shall allow him such remuneration as they think reasonable.

Accountability of Officers.

21.—(1) Every officer appointed by the council shall at such times during the continuance of his office, or within three months after his ceasing to hold it, and in such manner as the council direct, deliver to the council, or as they direct, a true account in writing of all matters committed to his charge, and of his receipts and payments, with vouchers, and a list of persons from whom money is due for purposes of this Act in connection with his office, showing the amount due from each.

(2) Every such officer shall pay all money due from him to the treasurer as the council direct.

(3) If any such officer—

(a) Refuses or wilfully neglects to deliver any account or list which he ought to deliver, or any voucher relating thereto, or to make any payment which he ought to make ; or

- (b) After three days' notice in writing, signed by the town clerk or by three members of the council, given or left at his usual or last known place of abode, refuses or wilfully neglects to deliver to the council, or as they direct, any book or document which he ought so to deliver, or to give satisfaction respecting it to the council, or as they direct ;

a court of summary jurisdiction having jurisdiction where the officer is or resides may, by summary order, require him to make such delivery or payment, or to give such satisfaction.

- (4) But nothing in this section shall affect any remedy by action against any such officer or his surety, except that the officer shall not be both sued by action and proceeded against summarily for the same cause.

ACCOUNTS AND AUDIT.

The Borough Auditors.

25.—(1) There shall be three Borough Auditors, two elected by the burgesses, called Elective Auditors, and one appointed by the mayor, called Mayor's Auditor.

- (2) An Elective Auditor must be qualified to be a councillor, but may not be a member of the council, or the town clerk, or the treasurer,

- (3) The Mayor's Auditor must be a member of the council.

- (4) The term of office of each Auditor shall be one year.

- (5) The appointment of the Mayor's Auditor shall be made on the ordinary day of election of the Elective Auditors.

- (6) On a casual vacancy in his office an appointment to fill it shall be made within ten days after the occurrence of the vacancy.

Audit and Publication of Treasurer's Accounts.

27.—(1) The treasurer shall, within one month from the date to which he is required to make up his accounts in each half-year, submit them, with the necessary vouchers and papers to the Borough Auditors, and they shall audit them.

- (2) After the audit of the accounts for the second half of each financial year the treasurer shall print a full abstract of his accounts for that year.

Returns to Local Government Board.

28.—(1) The town clerk shall make a return to the Local Government Board of the receipts and expenditure of the municipal corporation for each financial year.

(2) The return shall be made for the financial year ending on the twenty-fifth of March, or on such other day as the Local Government Board, on the application of the council, from time to time prescribe.

(3) The return shall be in such form and contain such particulars as the Local Government Board from time to time direct.

(4) The return shall be sent to the Local Government Board within one month after the completion of the audit for the second half of each financial year.

(5) If the town clerk fails to make any return required under this section he shall for each offence be liable to a fine not exceeding twenty pounds, to be recovered by action on behalf of the Crown in the High Court.

(6) The Local Government Board shall in each year prepare an abstract of the returns made in pursuance of this section, under general heads, and it shall be laid before both Houses of Parliament.

CORPORATE LAND.

Power to Purchase Land for Town Hall, &c.

105.—A municipal corporation may contract for the purchase of and hold any land not exceeding in the whole five acres, either in or out of the borough, and thereon, or on any land belonging to or held in trust for the corporation, may build a town hall, council house, justices' room, with or without a police station and cells, or lock-ups, or a quarter and petty sessions house, or an assize court-house, with or without judges' lodgings, or a polling station, or any other building necessary or proper for any purpose of the borough.

Power to Borrow with approval of Treasury.

106.—The council may, with the approval of the Treasury, borrow at interest on the security of any corporate land, or of any land proposed to be purchased by the council under this Act, or of the borough fund or borough rate, or of all or any of those securities, such sums as the council from time to time think requisite for the purchase of land, or for the building of any building which the council are by this Act authorised to build.

Restrictions on alienation of Corporate Land without approval of Treasury.

108.—(1) The council shall not, unless authorised by Act of Parliament, sell, mortgage, or alienate any corporate land without the approval of the Treasury.

(2) The council shall not, unless authorised by Act of Parliament, lease or agree to lease any corporate land without the approval of the Treasury, except as follows :—

- (a) They may make a lease or agreement for a lease for a term not exceeding thirty-one years from the date of the lease or agreement, so that there be reserved and made payable during the whole of the term such clear yearly rent as to the council appears reasonable, without any fine.
- (b) They may make a lease or agreement for a lease for a term not exceeding seventy-five years from the date of the lease or agreement and either at a reserved rent or on a fine, or both, as the council think fit,—
- (i.) Of tenements or hereditaments, the greater part of the yearly value of which, at the date of the lease or agreement, consists of any building or buildings ; or
- (ii.) Of land proper for the erection of any houses or other buildings thereon, with or without gardens, yards, curtilages, or other appurtenances to be used therewith ; or
- (iii.) Where the lessee or intended lessee agrees to erect a building or buildings thereon of greater yearly value than the land,—of land proper for gardens, yards, curtilages, or other appurtenances to be used with any other house or other building erected or to be erected on any such land, belonging either to the corporation or to any other proprietor, or proper for any other purpose calculated to afford convenience or accommodation to the occupiers of any such house or building.

WORKING MEN'S DWELLINGS.

Sites for Working Men's Dwellings.

III.—(1) If a municipal corporation determines to convert any corporate land into sites for working men's dwellings, and obtains the approval of the Treasury for so doing, the corporation may, for that purpose, make grants or leases for terms of nine hundred and ninety-nine years, or any shorter term, of any parts of the corporate land.

(2) The corporation may make on the land any roads, drains, walls, fences, or other works requisite for converting the same into building land at an expense not exceeding such sum as the Treasury approve.

(3) The corporation may insert in any grant or lease of any part of the land (in this section referred to as the site) provisions binding the grantee or lessee to build thereon as in the grant or lease prescribed, and to

maintain and repair the building, and prohibiting the division of the site or building, and any addition to or alteration of the character of the building, without the consent of the corporation, and for the re-vesting of the site in the corporation, or its entry thereon, on breach of any provision in the grant or lease.

(4) Every such provision shall be valid in law to all intents, and binding on the parties.

(5) All costs and expenses incurred or authorised by a corporation in carrying into execution or otherwise in pursuance of this section, shall be paid out of the borough fund and borough rate, or by money borrowed by the corporation under this Part.

(6) In this section the term "working men's dwellings" means buildings suitable for the habitation of persons employed in manual labour and their families; but the use of part of a building for purposes of retail trade or other purposes approved by the council shall not prevent the building from being deemed a dwelling.

REPAYMENT OF LOANS.

Power for Treasury to Impose Conditions as to Repayment of Money Borrowed.

112.—(1) Where the Treasury approve a mortgage or charge under this Part they may, as a condition of their approval, require that the money borrowed on the security of the mortgage or charge be repaid, with all interest thereon, in thirty years, or any less period, and either by instalments or by means of a sinking fund, or both.

(2) In that case the sums required for providing for the repayment of the principal and interest of the money borrowed shall be by virtue of this Act a charge on all or any of the following securities, namely, the land comprised in the mortgage (without prejudice to the security thereby created), or any other corporate land, or the borough fund or the borough or other rates legally applicable to payment of the money borrowed or of the expenses which the money is borrowed to defray, as the Treasury direct.

LOANS FOR MUNICIPAL BUILDINGS.

Power to Borrow for Buildings.

120.—The council of a borough may borrow money from the Public Works Loan Commissioners for the purpose of building, enlarging, repairing, improving, and fitting up any building which they are by this Act authorised to build, and may levy a rate or an increase of the borough rate for the purpose of paying the principal and interest of the

loan, and may mortgage the rate or borough rate to the Commissioners in accordance with the Public Works Loans Act 1875, or any amendment thereof, in such manner and form as the Commissioners direct.

BOROUGH FUND.

Payments to Borough Fund.

139.—The rents and profits of all corporate land, and the interest, dividends, and annual proceeds of all money, dues, chattels, and valuable securities belonging or payable to a municipal corporation, or to any member or officer thereof in his corporate capacity, and every fine or penalty for any offence against this Act (except where and as far as the application thereof is otherwise provided for) shall go to the borough fund.

Application of Borough Fund.

140.—(1) The borough fund shall be applicable to and charged with the several payments specified in the Fifth Schedule.

(2) The payments specified in Part I. of that schedule may be made without order of the council; those specified in Part II. may not be made without such order.

(3) No other payment shall be made out of the borough fund, except—

(a) Under the authority of an Act of Parliament; or

(b) By order of the Council; or

(c) By order of the Court of Quarter Sessions for the borough; or

(d) By order of a justice in pursuance of this Act; or

(e) In cases in which the Court of Quarter Sessions for a county, or a justice acting in and for a county in the discharge of his judicial duty, might make an order for the payment of money on the treasurer of the county.

(4) Saving, nevertheless, in relation to the application of the borough fund as authorised by this section, or otherwise by this Act, all rights, interests, and demands of all persons in or on the real or personal estate of the municipal corporation, by virtue of any legal proceeding, or of any mortgage, or otherwise.

Payments to and by Treasurer.

142.—(1) All payments to and out of the borough fund shall be made to and by the treasurer.

(2) All payments to the treasurer shall go to the borough fund.

Application of Surplus of Borough Fund.

143.—(1) If the borough fund is more than sufficient for the purposes to which it is applicable under this Act, or otherwise by law, the surplus thereof shall be applied under the direction of the council for the public benefit of the inhabitants and improvements of the borough.

(2) If the surplus arises from the rents and profits of the property of the municipal corporation, and not from a borough rate, and the borough is a sanitary district under the Public Health Act 1875, then the municipal corporation, as the sanitary authority for the borough, may apply the surplus in payment of any expenses incurred by them as such sanitary authority before or after the commencement of this Act, in improving the borough, or any part thereof, by drainage, enlargement of streets, or otherwise, under the Public Health Act 1875, or any Act thereby repealed.

BOROUGH RATE.

Power for Council to make Borough Rate, and assess Contribution thereto.

144.—(1) If the borough fund is insufficient for the purposes to which it is applicable under this Act or otherwise by law, the council shall from time to time estimate, as correctly as may be, what amount, in addition to the borough fund, will be sufficient for those purposes.

(2) In order to raise that amount, the council shall, subject to the provisions of this Act, from time to time order a rate, called a borough rate, to be made in the borough.

(3) A borough rate may be made retrospectively, in order to raise money for the payment of charges and expenses incurred, or which have come in course of payment, at any time within six months before the making of the rate.

(4) The council shall assess the contributions to the borough rate on the several parishes and parts of parishes in the borough in proportion to the total annual value of the hereditaments in each parish or part which are rateable to the poor, or in respect of which a contribution is made to the poor rate.

(5) That value shall be estimated according to the valuation list (if any) in force for the time being, and if there is none, according to the last poor rate.

(6) But if for any reason the council think that the valuation list or poor rate is not a fair criterion of value they may cause an independent valuation to be made.

(7) For the purpose of assessing a borough rate, or for the purpose of an independent valuation, the council from time to time may cause any of the books of assessment of any rates or taxes, Parliamentary or parochial,

on any property, and the valuation by which the assessment is made, in the hands of the overseers, to be brought before them, and may take copies thereof or extracts therefrom, or may direct any person to take copies of or extracts from such books being in his hands, without having the same brought before the council, or may call before them any overseer to give evidence respecting the same; and may cause copies of the total amount assessed in each parish in respect of any tax payable to the Crown, and the total amount of the valuation of the property on which that assessment was made in any past year, to be made out by the clerk to the commissioners of each district.

(8) The overseers and such persons as they select, by warrant of the council, signed by the mayor and sealed with a corporate seal, may enter on, view, and examine any land chargeable to the borough rate, in order to ascertain the annual value at which it ought to be charged; but no such entry shall in any case be made unless fourteen days' previous notice in writing, signed by the mayor and sealed with the corporate seal, of the intention to make the entry, has been given to the overseers and to the persons on whose land the entry is to be made.

(9) If on any occasion the overseers of a parish think that their parish is aggrieved by a borough rate, on account of the proportions assessed as the contributions of the respective parishes being unequal, or on account of some parish being without sufficient cause omitted, or on account of any other just cause of complaint, they may appeal to the recorder at the next quarter sessions for the borough, or if there is none, to the next quarter sessions for the county wherein the borough is situate, or whereto it is adjacent, against such part of the rate only as affects their parish.

(10) The recorder or quarter sessions shall hear and finally determine the appeal, and either confirm such parts of the rate as are appealed against, or correct any inequalities, disproportions or omissions proved to exist therein, as to him or them appears just.

(11) The expenses of the appeal shall be paid by such parishes or persons and in such proportions as the recorder or court having cognisance of the appeal directs.

(12) If any person having custody of any book for which the council call under this section fails to produce it to the council, or to permit any copy thereof or extract therefrom to be made or taken, or to give such evidence as the council require, he shall, on summary conviction, be liable to a fine not exceeding ten pounds.

(13) If any clerk to the commissioners of a district fails to make any copy, which he is required to make under this section, within a reasonable time after his receipt of the order to make it, he shall, on summary conviction, be liable to a fine not exceeding twenty pounds.

THE LOCAL GOVERNMENT ACT, 1888.

51 and 52 Vict. c. 41.

68.—(1) All receipts of the County Council, whether for general or special county purposes, shall be carried to the county fund, and all payments for general or special county purposes shall be made in the first instance out of that fund.

(2) In this Act the expression "general county purposes," means all purposes declared by this or any other Act to be general county purposes, and all purposes for contributions to which the County Council are for the time being authorised by law to assess the whole area of their administrative county: and the expression "general county account" means the account of the county fund to which the contributions so raised are carried, and any costs incurred for a general county purpose shall be general expenses, and all costs incurred by the County Council in the execution of their duties which are not by law made special expenses shall be general expenses.

(3) In this Act the expression "special county purposes" means any purposes from contribution to which any portion of the county is for the time being exempt, and also includes any purposes where the expenditure involved is by law restricted to a hundred, division, or other limited part of the county, and the expression "special county account" means any account of the county fund to which contributions for special county purposes are carried, and any costs incurred for a special county purpose shall be special expenses.

(4) If the moneys standing to the general county account of the county fund are insufficient to meet the expenditure for general county purposes, county contributions may be levied to meet the deficiency on the whole administrative county, and shall be assessed on all the parishes in the county.

(5) If the moneys standing to any special county account of the county fund are insufficient to meet the expenditure for the special county purposes chargeable to that account, county contributions may be levied to meet the deficiency on any parishes in the county liable to be assessed to county contributions for those purposes.

(7) The County Council shall keep such accounts as will prevent the whole administrative county from being charged with expenditure properly payable by a portion only of the county, and will prevent any sums raised in a portion only of the county being applied in reduction of expenditure properly payable by the whole or a larger part of the

county and will prevent any sums by law specifically applicable to any particular purpose from being applied to any other purpose.

(9) County contributions may be made retrospective in order to raise money for the payment of costs incurred or having become payable at any time within six months before the demand of the contributions.

71.—(1) The accounts of the receipts and expenditure of County Councils shall be made up to the end of each local financial year as defined by this Act, and be in the form for the time being prescribed by the Local Government Board.

(3) The accounts of a County Council and of the county treasurer and officers of such council shall be audited by the district Auditors appointed by the Local Government Board in like manner as accounts of an urban authority and their officers under sections two hundred and forty-seven and two hundred and fifty of the Public Health Act 1875.

74.—(1) At the beginning of every local financial year, every County Council shall cause to be submitted to them an estimate of the receipts and expenses of such council during that financial year, whether on account of property, contributions, rates, loans, or otherwise.

(2) The council shall estimate the amount which will require to be raised in the first six months and in the second six months of the said financial year by means of contributions.

(3) If at the expiration of the first six months of such financial year it appears to the council that the amount of contribution, or rate estimated at the commencement of the year, will be larger than is necessary, or will be insufficient, the council may revise the estimate and alter accordingly the amount of the contribution or rate.

8c.—(1) All payments to and out of the county fund shall be made to and by the county treasurer, and all payments out of the fund shall, unless made in pursuance of the specific requirement of an Act of Parliament, or of an order of a competent Court, be made in pursuance of an order of the council, signed by three members of the finance committee, present at the meeting of the council, and countersigned by the clerk of the council, and the same order may include several payments.

(3) Every County Council shall from time to time appoint a finance committee for regulating and controlling the finance of their county; and the order for the payment of a sum out of the county fund, whether

on account of capital or income, shall not be made by a County Council, except in pursuance of a resolution of the Council passed on the recommendation of the finance committee, and (subject to the provisions of this Act respecting the standing joint committee) any costs, debt, or liability exceeding fifty pounds shall not be incurred except upon a resolution of the council, passed on an estimate submitted by the finance committee.

THE LOCAL GOVERNMENT ACT, 1894.

56 and 57 Vict. c. 37.

58.—(1) The accounts of the receipts and payments of parish and district councils, and of parish meetings for parishes not having parish councils, and their committees and officers, shall be made up yearly to the thirty-first day of March, or in the case of accounts which are required to be audited half-yearly, then half-yearly to the thirtieth day of September and the thirty-first day of March in each year, and in such form as the Local Government Board prescribe.

(2) The said accounts shall, except in the case of accounts audited by the Auditors of a borough (but inclusive of the accounts of a joint committee appointed by a borough council with another council not being a borough council), be audited by a District Auditor, and the enactments relating to audit by District Auditors of accounts of urban sanitary authorities and their officers, and to all matters incidental thereto and consequential thereon, shall apply accordingly, except that in the case of the accounts of rural district councils, their committees and officers, the audit shall be half-yearly instead of yearly.

(3) The Local Government Board may, with respect to any audit to which this section applies, make rules modifying the enactments as to publication of notice of the audit, and of the abstract of accounts and the report of the Auditor.

(4) Every parochial elector of a rural parish may, at all reasonable times, without payment, inspect and take copies of and extracts from all books, accounts, and documents belonging to or under the control of the parish council of the parish or parish meeting.

(5) Every parochial elector of a parish in a rural district may at all reasonable times, without payment, inspect and take copies of and extracts from all books, accounts, and documents belonging to or under the control of the district council of the district.

89.—The Acts specified in the second schedule to this Act are hereby repealed as from the appointed day to the extent in the third column of that schedule mentioned, and so much of any Act, whether public, general, or local and personal, as is inconsistent with this Act is also hereby repealed. . . .

FORM A.

[Form of Statement to be used when none of the Adoptive Acts are in force, and the Parish Council have no Financial transactions with regard to Charities.]

Parish Council for the Parish of

In the Rural District of

In the Administrative County of

FINANCIAL STATEMENT.

THE DISTRICT AUDITORS ACT, 1879 (42 Vict. c. 6),

AND

THE LOCAL GOVERNMENT ACT, 1894 (56 & 57 Vict. c. 73).

STATEMENT OF RECEIPTS AND PAYMENTS of the Parish Council for the above-named Parish for the period ended the 31st day of March 1895.

*Name of Clerk (or other person } _____
keeping the Accounts) }*

Office Address _____

Post Town _____

A—continued.

Parish Council for the Parish of

Council administering none of the Adoptive Acts (see sec. 7 of the no accounts in regard to Charities.)

I. PAYMENTS.

PAYMENTS OTHER THAN OUT OF LOANS.

Payments to Joint Committees or other Local Authorities (<i>naming them</i>):—		£	s	d	£	s	d
Name of Authority	On what Account	£ s d					
<p>(The sums entered against the following headings are not to include payments to other Local Authorities. See headings above.)</p> <p>Salaries of Officers</p> <p>* Establishment Charges</p> <p>Cost of Meetings, Polls, and Elections</p> <p>† Allotments</p> <p>† Footpaths and Rights of Way</p> <p>† Commons, Open Spaces, Public Walks and Recreation Grounds, and Works connected therewith</p> <p>† Fire Engine and Fire Escape</p> <p>† Maintenance and Repair of Parish Property not specified under other headings</p> <p>Other Payments (<i>specifying them</i>):—</p>		£ s d					
Total Payments		£					
Balance in hand at the end of the year ..		£					
TOTAL PAYMENTS AND BALANCE ..		£					

* The cost of Stationery, Printing, Books, Postage, and Office Rent, Rates, and Taxes should be entered against this heading.

† Where Salaries are paid exclusively to Officials employed on these or any other of the works and purposes enumerated on this page, the amounts of such salaries should be included in the items entered under the heading relating to the work or purpose, and not under the heading "Salaries of Officers."

FORM A—*continued.*

PART II.

SUMMARY of the Receipts and Payments shown in the foregoing Statement.

Receipts :—	£ s d
Payments :—	_____
Deduct :— Payments under Precept to other Local Authorities, if any, viz. :—	£ s d _____
Net Expenditure on which Stamp Duty is payable	£ _____

_____ { Clerk to Parish Council, or
Chairman of Parish Council.

This _____ day of _____ 1895.

TOTAL PAYMENTS as shown above	£ s d
Less Amount disallowed at Audit	_____
AMOUNT ALLOWED AT AUDIT	_____

I HEREBY CERTIFY that I have compared the entries in this Financial Statement with the Vouchers and other Documents relating thereto, and that the regulations with respect to such Statement have been duly complied with.

I HEREBY FURTHER CERTIFY that I have ascertained by Audit the correctness of such Statement, and that the amount expended by the Parish Council during the period ended the 31st day of March 1895, as included in such Statement, and allowed by me at the Audit, is *

_____ STAMP _____ District Auditor.

* The amount to be inserted in words at length.

EDUCATION ACT, 1902.

2 *Edw. 7, c. 42.*

PART I.

Local Education Authority.

1.—For the purposes of this Act the council of every county and of every county borough shall be the local education authority :

Provided that the council of a borough, with a population of over ten thousand, or of an urban district with a population of over twenty thousand shall, as respects that borough or district, be the local education authority for the purpose of Part III. of this Act, and for that purpose as respects that borough or district, the expression "local education authority" means the council of that borough or district.

Aid Grant.

10.—(1) In lieu of the grants under the Voluntary Schools Act 1897, and under section ninety seven of the Elementary Education Act 1870, as amended by the Elementary Education Act 1897, there shall be annually paid to every local education authority, out of moneys provided by Parliament—

- (a) a sum equal to four shillings per scholar ; and
- (b) an additional sum of three half-pence per scholar for every complete twopence per scholar by which the amount which would be produced by a penny rate on the area of the authority falls short of ten shillings a scholar : Provided that, in estimating the produce of a penny rate in the area of a local education authority not being a county borough, the rate shall be calculated upon the county rate basis, which, in cases where part only of a parish is situated in the area of the local education authority, shall be apportioned in such manner as the Board of Education think just.

But if in any year the total amount of Parliamentary grants payable to a local education authority would make the amount payable out of other sources by that authority on account of their expenses under this Part of this Act less than the amount which would be produced by a rate of threepence in the pound, the Parliamentary grants shall be decreased, and the amount payable out of other sources shall be increased by a sum equal in each case to half the difference.

(2) For the purposes of this section the number of scholars shall be taken to be the number of scholars in average attendance, as computed by the Board of Education, in public elementary schools maintained by the authority.

Expenses.

18.—(1) The expenses of a council under this Act shall, so far as not otherwise provided for, be paid, in the case of the council of a county out of the county fund, and in the case of the council of a borough out of the borough fund or rate, or, if no borough rate is levied, out of a separate rate to be made, assessed, and levied in like manner as the borough rate, and in the case of the council of an urban district other than a borough in manner provided by section thirty-three of the Elementary Education Act 1876 as respects the expenses mentioned in that section: Provided that—

- (a) the county council may, if they think fit (after giving reasonable notice to the overseers of the parish or parishes concerned), charge any expenses incurred by them under this Act with respect to education other than elementary on any parish or parishes which, in the opinion of the council, are served by the school or college in connection with which the expenses have been incurred; and
- (b) the county council shall not raise any sum on account of their expenses under Part III. of this Act within any borough or urban district the council of which is the local education authority for the purposes of that Part; and
- (c) the county council shall charge such portion as they think fit, not being less than one-half or more than three-fourths, of any expenses incurred by them in respect of capital expenditure or rent on account of the provision or improvement of any public elementary school on the parish or parishes which, in the opinion of the council, are served by the school; and
- (d) the county council shall raise such portion as they think fit, not being less than one-half or more than three-fourths, of any expenses incurred to meet the liabilities on account of loans or rent of any school board transferred to them, exclusively within the area which formed the school district in respect of which the liability was incurred, so far as it is within their area.

(2) All receipts in respect of any school maintained by a local education authority, including any Parliamentary grant, but excluding sums specially applicable for purposes for which provision is to be made by the managers, shall be paid to that authority.

(3) Separate accounts shall be kept by the council of a borough of their receipts and expenditure under this Act, and those accounts shall be made up and audited in like manner and subject to the same provisions as the accounts of a county council, and the enactments relating to the audit of those accounts and to all matters incidental thereto and

consequential thereon, including the penal provisions, shall apply in lieu of the provisions of the Municipal Corporations Act 1882 relating to accounts and audit.

(4) Where under any local Act the expenses incurred in any borough for the purposes of the Elementary Education Acts 1870 to 1900 are payable out of some fund or rate other than the borough fund or rate, the expenses of the council of that borough under this Act shall be payable out of that fund, or rate instead of out of the borough fund or rate.

(5) Where any receipts or payments of money under this Act are entrusted by the local education authority to any education committee established under this Act, or to the managers of any public elementary school, the accounts of those receipts and payments shall be accounts of the local education authority, but the auditor of those accounts shall have the same power with respect to managers as he would have if the managers were officers of the local education authority.

Borrowing.

19.—(1) A council may borrow for the purposes of the Elementary Education Acts 1870 to 1900, or this Act, in the case of a county council as for the purposes of the Local Government Act 1888, and in the case of the council of a county borough, borough, or urban district as for the purposes of the Public Health Acts, but the money borrowed by a county borough, borough, or urban district council shall be borrowed on the security of the fund or rate out of which the expenses of the council under this Act are payable.

(2) Money borrowed under this Act shall not be reckoned as part of the total debt of a county for the purposes of section sixty-nine of the Local Government Act 1888, or as part of the debt of a county borough, borough, or urban district for the purpose of the limitation on borrowing under sub-sections two and three of section two hundred and thirty-four of the Public Health Act 1875.

EDUCATION (LONDON) ACT, 1903.

3 Edw. 7, c. 24.

1.—The Education Act 1902 (in this Act referred to as the principal Act) shall, so far as applicable, and subject to the provisions of this Act, apply to London.

4.—(1) The modifications of the principal Act set out in the first Schedule to this Act shall have effect for the purposes of this Act.

(2) The expression "metropolitan borough" in this Act shall include the City, and the expression "council of a metropolitan borough" shall include the mayor, aldermen, and commons of the city of London in common council assembled.

FIRST SCHEDULE.

4.—The provisoes to sub-section one of section eighteen of the principal Act (relating to expenses), and sub-section two of section thirteen of that Act (relating to endowments), shall not apply, but the Board of Education may, on the application of the Trustees of the endowment, or of the local education authority, direct that any money which would be payable under the said section thirteen to the county council shall be applied in manner provided by a scheme made by the Board if the Board consider that it is expedient to make such a scheme. In any such scheme due regard shall primarily be had to the interests of the locality for which the benefits of the endowment were intended.

5.—The words "a county council" in section nineteen of the principal Act (which relates to borrowing) shall, as respects borrowing by the local education authority, be construed as if they were "the London County Council."

JUDICIAL TRUSTEES ACT, 1896.

59 and 60 Vict. c. 35.

1.—(1) Where application is made to the Court by or on behalf of the person creating or intending to create a trust, or by or on behalf of a trustee or beneficiary, the Court may, in its discretion, appoint a person (in this Act called a judicial trustee) to be a trustee of that trust, either jointly with any other person or as sole trustee, and, if sufficient cause is shown, in place of all or any existing trustees.

(2) The administration of the property of a deceased person, whether a testator or intestate, shall be a trust, and the executor or administrator a trustee, within the meaning of this Act.

(3) Any fit and proper person nominated for the purpose in the application may be appointed a judicial trustee, and, in the absence of such nomination, or if the Court is not satisfied of the fitness of a person so nominated, an official of the Court may be appointed, and in any case a judicial trustee shall be subject to the control and supervision of the Court as an officer thereof.

(4) The Court may, either on request or without request, give to a judicial trustee any general or special directions in regard to the trust or the administration thereof.

(5) There may be paid to a judicial trustee out of the trust property such remuneration, not exceeding the prescribed limits, as the Court may assign in each case, subject to any rules under this Act respecting the application of such remuneration where the judicial trustee is an official of the Court, and the remuneration so assigned to any judicial trustee shall, save as the Court may for special reasons otherwise order, cover all his work and personal outlay.

(6) Once in every year the accounts of every trust of which a judicial trustee has been appointed shall be audited, and a report thereon made to the Court by the prescribed persons, and, in any case where the Court shall so direct, an inquiry into the administration by a judicial trustee of any trust, or into any dealing or transaction of a judicial trustee, shall be made in the prescribed manner.

2.—The jurisdiction of the Court under this Act may be exercised by the High Court, and as respects trusts within its jurisdiction by a Palatine Court, and (subject to the prescribed definition of the jurisdiction) by any County Court Judge to whom such jurisdiction may be assigned under this Act.

THE APPORTIONMENT ACT, 1870.

33 and 34 Vict. c. 35.

2.—From and after the passing of this Act, all rents, annuities, dividends, and other periodical payments in the nature of income (whether reserved or made payable under an instrument in writing or otherwise) shall, like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly.

5.—In the construction of this Act :—

The word "rents" includes rent service, rent charge, and rent seek, and all tithes and all periodical payments or renderings in lieu of or in the nature of rent or tithe.

The word "annuities" includes salaries and pensions.

The word "dividends" includes (besides dividends strictly so called) all payments made by the name of dividend, bonus, or otherwise out of the revenue of trading or other public companies, divisible between all or any of the members of such respective companies,

whether such payments shall be usually made or declared at any fixed times or otherwise; and all such divisible revenue shall, for the purposes of this Act, be deemed to have accrued by equal daily increment during and within the period for or in respect of which the payment of the same revenue shall be declared or expressed to be made; but the said word "dividend" does not include payments in the nature of a return or reimbursement of capital.

6.—Nothing in this Act contained shall render apportionable any annual sums made payable in policies of assurance of any description.

7.—The provisions of this Act shall not extend to any case in which it is or shall be expressly stipulated that no apportionment shall take place.

THE INTESTATES' ESTATES ACT, 1890.

53 and 54 Vict. c. 29.

1.—The real and personal estates of every man who shall die intestate after the first day of September one thousand eight hundred and ninety, leaving a widow but no issue shall, in all cases where the net value of such real and personal estates shall not exceed five hundred pounds, belong to his widow absolutely and exclusively.

2.—Where the net value of the real and personal estates in the preceding section mentioned shall exceed the sum of five hundred pounds, the widow of such intestate shall be entitled to five hundred pounds part thereof absolutely and exclusively, and shall have a charge upon the whole of such real and personal estates for such five hundred pounds, with interest thereon from the date of the death of the intestate at four per cent. per annum until payment.

3.—As between the real and personal representatives of such intestate such charge shall be borne and paid in proportion to the values of the real and personal estates respectively.

4.—The provision for the widow intended to be made by this Act shall be in addition and without prejudice to her interest and share in the residue of the real and personal estates of such intestate remaining after payment of the sum of five hundred pounds, in the same way as if such residue had been the whole of such intestate's real and personal estates and this Act had not been passed.

5.—The net value of such real estates as aforesaid shall for the purpose of this Act be estimated in the case of a fee simple upon the basis of twenty years' purchase of the annual value by the year at the date of the

death of the intestate as determined by law for the purposes of property tax, less the gross amount of any mortgage or other principal sum charged thereon, and less the value of any annuity or other periodical payment chargeable thereon to be valued according to the tables and rules in the schedule annexed to the statute sixteenth and seventeenth Victoria, chapter fifty-one, and in the case of an estate for a life or lives according to the said tables and rules.

6.—The net value of such personal estate as aforesaid shall be ascertained by deducting from the gross value thereof all debts, funeral and testamentary expenses of the intestate, and all other lawful liabilities and charges to which the said personal estate shall be subject.

8.—This Act shall not extend to Scotland.

The rules by which the estate of intestates is distributed are given below.

PERSONAL ESTATE.

If the intestate die leaving—

Wife and Child, or Children.—One-third to wife, rest to child or children, to be divided equally amongst them, and if children are dead, then to the representatives (that is, their lineal descendants); except such child or children, not heirs-at-law, who had estate by settlement of intestate, or were advanced by him, in which case exceptional rules apply.

Wife † only, no blood relation.—Half to wife, other half to the Crown.

Wife, † no near relations.—Half to wife, rest to those next-of-kin equal in degree to intestate.

No Wife or Child.—All to next-of-kin.

No Wife, but Child, Children, or representatives of them, whether such Child or Children by one or more Wives.—All to him, her, or them.

Children by two Wives.—Equally to all.

If no Child, Children or representatives of them.—All to next-of-kin in equal degree to intestate.

Child and Grandchild by deceased Child.—Half to child, half to grandchild who takes by representation.

Husband.—Whole to him.

Father, and Brother or Sister.—Whole to father.

† In all these cases the wife is entitled to a clear £500 in addition to her share, such sum being a charge upon the realty and the personalty rateably. If the estate does not exceed £500 in value she takes the whole. (Intestacy Act, 1890.)

Mother, and Brother or Sister.—Whole to them divided equally.

Wife,† Mother, Brother, Sisters, and Nieces.—Half to wife, residue to mother, brothers, sisters, and nieces.

Wife,† and Father.—Half to wife and half to father.

Wife,† Mother, Nephews, and Nieces.—Half to wife, one-fourth to mother, and other fourth to nephews and nieces.

Wife,† Brothers, or Sisters, and Mother.—Half to wife, half to brothers or sisters and mother.

Mother, but no Wife, Child, Father, Brother, Sister, Nephew, or Niece.—The whole to mother.

Wife† and Mother.—Half to wife and half to mother.

Brother or Sister of whole blood, and Brother or Sister of half blood.—Equally to both.

Posthumous Brother or Sister and Mother.—Equally to both.

Posthumous Brother or Sister and Brother or Sister born in lifetime of Father.—Equally to both.

Father's Father and Mother's Mother.—Equally to both.

Uncle's or Aunt's Children and Brother's or Sister's Grandchildren.—Equally to all.

Grandmother, Uncle, or Aunt.—All to grandmother.

Two Aunts, Nephew, and Niece.—Equally to all.

Uncle and deceased Uncle's Child.—All to uncle.

Uncle by Mother's side and deceased Uncle's or Aunt's Child.—All to uncle.

Nephew by Brother, and Nephew by Half-sister.—Equally *per capita*.*

Nephew by deceased Brother and Nephews and Nieces by deceased Sister.—Each in equal shares *per capita*, and not *per stirpes*.

Brother and Grandfather.—Whole to brother.

Brother's Grandson, and Brother's or Sister's Daughter.—All to daughter.

Brother and two Aunts.—All to brother.

Brother and Wife.—Half to brother, half to wife.

Mother and Brother.—Equally.

Wife,† Mother and Children of a deceased Brother (or Sister).—Half to wife, a fourth to mother, and a fourth *per stirpes* to deceased brothers or sister's children.

* That is, taking individually and not by representation. Thus, if A. die, leaving three brothers, or sisters, they each take an equal part of his effects, in his or her own right. But if either of them die, leaving children, his children would take his share *per stirpes*, that is, *through him*, and not in their own rights.

By the Act 19 and 20 Vict. all special *local* customs relating to intestate's estates are abolished.

Wife,† Brother or Sister, and Children of a deceased Brother or Sister.—Half to wife, one-fourth to brother or sister *per capita*, one-fourth to deceased brother's or sister's children *per stirpes*.

Brother or Sister and Children of a deceased Brother or Sister.—Half to brother or sister *per capita*, half to children of deceased brother or sister *per stirpes*.

Grandfather, no nearer relation.—All to grandfather.

REAL ESTATE.

No illegitimate child is capable of inheriting real estate. (Custom of Gavelkind (descent to all sons alike) still exists in Kent, and custom of Borough English (descent to youngest son) in divers ancient boroughs. Custom of London for Administration of Personal Estate abolished in 1856. Leaseholds are Personal Estate. The Dower (*viz.*, widow's thirds) of widows married since 1833 is in the majority of cases barred by the purchase deed. Generally put in by solicitors to avoid the inconvenience of dower attaching.

In each instance it is supposed that there are no nearer relations than those named.

(*The persons named within brackets are those who are entitled to administer.*)

If intestate die leaving—

Wife only, no blood relations.—Real property would descend one-third to wife for life, rest to Crown; copyholds to lord of manor. [*Wife.*]

Wife and Child, or Children, and Children of a deceased Child.—One-third to wife for life; rest to eldest son or his issue. [*Wife.*]

One-third to wife for life in any case. [*Wife.*]

Rest to eldest son or his issue, such son and his issue, whether male or female, being preferred to any other son and his issue, and all sons and their issue, whether male or female, being preferred to all daughters and their issue, whether male or female.

If no son, rest to daughters equally. [*Either daughter, or not exceeding three.*]

If daughters and grandchildren (sons and daughters of deceased daughter) rest to daughters, and eldest son of deceased daughter.

Wife and Father.—One-third to wife for life; rest to father, if deceased purchased same or had it left him by will. [*Wife.*]

Wife and Mother.—One-third to wife for life; rest to mother, there being no heirs on father's side. [*Wife.*]

Wife, Brother or Sister, and Children of a deceased Brother or Sister.—One-third to wife for life in any case, rest to eldest brother or his issue. (See above, "Rest to eldest son or his issue," under head "Wife and child," &c.). [*Wife.*]

Wife, Brother, or Sister, and Children of a deceased Brother or Sister.—Sister and children of deceased sister, rest equally between sister and nephew (eldest). [*Wife.*]

Sisters and nieces only, children of deceased sister, rest equally between nieces, [*Wife.*]

Wife, Mother, Nephews, and Nieces.—One-third to wife for life; rest to nephew (eldest), or nieces, if brother left no son. [*Wife.*]

Wife, Mother, Brother, Sisters and Nieces (Children of deceased Brothers and Sisters).—One-third to wife for life in any case; rest to eldest brother. [*Wife.*]

Rest to nieces equally, if children of elder brother deceased.

No Wife or Child or issue of a deceased Child.—Lineal ancestor paternal, males of whole blood first. [*Father or grandfather, as case may be.*]

Children by one or more Wives, and the issue of deceased Children.—All to eldest son or his issue. (See above, "Rest to eldest son or his issue," under head "Wife and child," &c.). [*Either sons or daughters, not exceeding three.*]

Daughters equally.

Husband and Child or Children.—Husband for life; afterwards to only child or to eldest son or issue of a deceased eldest son. [*Husband.*]

If all daughters, to them equally.

Mother, but no Wife, Child, or issue of a Child, Father, Brother, Sister, Nephew, or Niece, or more distant descendants of Father.—All to mother in default of lineal ancestors on the father's side, or issues of such ancestors. [*Mother.*]

Mother, and Brother and Sisters.—All to eldest brother. [*Mother.*]

Mother and Sisters.—All to sisters. [*Mother.*]

Father, and Brother and Sisters.—All to father. [*Father.*]

Child and Grandchild by deceased Child.—See above, "Rest to eldest son or his issue," under head "Wife and child," &c. [*Child.*]

Brother and Grandfather.—All to brother. [*Brother.*]

Brother's Grandson, and Brother or Sister's Daughter.—All to great nephew, if eldest brother's grandson. [*Niece.*] All to brother's daughter, if child of eldest brother.

Brother and two Aunts.—Brother, all. [*Brother.*]

Brother and Wife.—One-third to wife for life; rest to brother. [*Wife.*]

Grandfather (no nearer).—All to grandfather. [*Grandfather.*]

Father's Father and Mother's Mother.—All to father's father. [*Either, or both.*]

Grandmother and Uncle, or Aunt on Father's side (no nearer).—All to uncle or aunt. [*Grandmother.*]

Uncle, and deceased's Uncle's Child.—Uncle, unless deceased uncle was elder brother, when his child takes all. [*Uncle.*]

Uncle by Mother's side, and deceased Uncle or Aunt's Child.—Child of deceased uncle on father's side, or (if none) child of deceased aunt on father's side. [*Deceased uncle or aunt's children not exceeding three.*]

Two Aunts, Nephew, and Niece, Children of deceased Brother.—Nephew. [*Two Aunts.*]

Uncle or Aunt's Children, and Brother's Grandchildren through a Son.—Eldest brother's grandson, or if grand-daughters between them equally. [*Either, not exceeding three.*]

Nephew by Brother, and Nephew by Half-sister.—Nephew by brother. [*Either, or both.*]

Nephew by deceased Brother, and Nephews and Nieces by deceased Sister.—All to eldest nephew, son of deceased brother. [*To either of the nephews and nieces, not exceeding three.*]

BUILDING SOCIETY ACCOUNTS.

THE BUILDING SOCIETIES ACT, 1874.

37 and 38 Vict. c. 42.

13.—Any number of persons may establish a society under this Act, either terminating or permanent, for the purpose of raising by the subscriptions of the members a stock or fund for making advances to members out of the funds of the society, upon security of freehold, copyhold, or leasehold estate, by way of mortgage; and any society under this Act shall, so far as is necessary for the said purpose, have power to hold land with the right of foreclosure, and may from time to time raise funds by the issue of shares of one or more denominations, either paid up in full, or to be paid by periodical or other subscriptions, and with or without accumulating interest, and may repay such fund, when no longer required for the purposes of the society: Provided

always, that any land to which any such society may become absolutely entitled by foreclosure, or by surrender, or other extinguishment of the right of redemption, shall as soon afterwards as may be conveniently practicable be sold or converted into money.

14.—The liability of any member of any society under this Act in respect of any share upon which no advance has been made shall be limited to the amount actually paid or in arrear on such share, and in respect of any share upon which an advance has been made shall be limited to the amount payable thereon under any mortgage or other security, or under the rules of the society.

Power to Borrow.

15.—With respect to the borrowing of money by societies under this Act, the following provisions shall have effect:—

- (1) Any society under this Act may receive deposits or loans, at interest within the limits in this section provided, from the members or other persons, or from corporate bodies, joint stock companies or from any terminating building society to be applied to the purposes of the society:
- (2) In a permanent society the total amount so received on deposit or loan and not repaid by the society shall not at any time exceed two-thirds of the amount for the time being secured to the society by mortgages from its members:
- (3) In a terminating society the total amount so received and not repaid may either be a sum not exceeding such two-thirds as aforesaid, or a sum not exceeding twelve months' subscriptions on the shares for the time being in force:
- (4) Any deposits with or loans to a society under this Act made before the commencement of this Act in accordance with its certified rules are hereby declared to be valid and binding on the society, but no further deposits or loans shall be received by such society, except within the limits provided by this section:
- (5) Every Deposit Book or acknowledgment or security of any kind given for a deposit or loan by a society shall have printed or written therein or thereon the whole of the fourteenth and fifteenth sections of the present Act.

What Rules must Provide.

16.—The rules of every society hereafter established under this Act shall set forth:—

- (6) The manner of appointing, remunerating, and removing the board of directors or committee of management, Auditors, and other officers:

- (8) Provision for an annual or more frequent audit of the accounts, and inspection by the Auditors of the mortgages and other securities belonging to the society.

Investment of Surplus Funds.

25.—Any society under this Act may from time to time, as the rules permit, invest any portion of the funds of the society not immediately required for its purposes, upon real or leasehold securities, or in the public funds, or in or upon any Parliamentary stock or securities, or in or upon any stock or securities, payment of the interest on which is guaranteed by authority of Parliament, or in the case of terminating societies, with other societies under this Act; and for the purpose of investments in the public funds or upon security of copyhold or customary estate, the society, or the board of directors and committee of management thereof, may from time to time appoint and remove trustees.

Decease of Member or Depositor Intestate.

29.—If any member of or depositor with a society under this Act, having in the funds thereof a sum of money not exceeding fifty pounds, shall die intestate, then the amount due may be paid to the person who shall appear to the directors or committee of management to the society to be entitled under the Statute of Distributions to receive the same, without taking out letters of administration, upon the society receiving satisfactory evidence of death and a statutory declaration that the member or depositor died intestate, and that the person so claiming is entitled as aforesaid: Provided that, whenever the society after the decease of any member or depositor has paid any such sum of money to the person who at the time appeared to be entitled to the effects of the deceased, under the belief that he had died intestate, the payment shall be valid and effectual with respect to any demand from any other person as next-of-kin or as the lawful representative of such deceased member or depositor against the funds of the society, but, nevertheless, such next-of-kin or representative shall have his lawful remedy for the amount of such payment as aforesaid against the person who has received the same.

Annual Accounts.

40.—The secretary or other officer of every society under this Act shall, once in every year at least, prepare an account of all the receipts and expenditure of the society since the preceding statement, and a general statement of its funds and effects, liabilities and assets, showing the amounts due to the holders of the various classes of shares respectively, to depositors and creditors for loans, and also the balance due or outstanding on their mortgage securities (not including prospective interest), and the

amount invested in the funds or other securities; and every such account and statement shall be attested by the Auditors, to whom the mortgage deeds and other securities belonging to the society shall be produced, and such account and statement shall be countersigned by the secretary or other officer; and every member, depositor, and creditor for loans shall be entitled to receive from the society a copy of such account and statement, and a copy thereof shall be sent to the Registrar within fourteen days after the annual or other general meeting at which it is presented, and another copy thereof shall be suspended in a conspicuous place in every office of the society under this Act.

THE BUILDING SOCIETIES ACT, 1894.

57 and 58 Vict. c. 47.

Matters to be set forth in Rules.

1.—The rules of every society under the Building Societies Acts established or substituting a new set of rules for its existing rules after the passing of this Act shall be set forth—

- (a) The manner in which the stock or funds of the society is or are to be raised;
- (b) The terms upon which unadvanced subscription shares are to be issued; the manner in which the contributions are to be paid to the society, and withdrawn by the members, with tables, where applicable in the opinion of the Registrar, showing the amount due by the Society for principal and interest separately;
- (c) The terms upon which paid-up shares, if any, are to be issued and withdrawn, with tables, where applicable in the opinion of the Registrar, showing the amount due by the society for principal and interest separately;
- (d) Whether preferential shares are to be issued, and, if so, within what limits;
- (e) The manner in which advances are to be made and repaid; the deductions, if any, for premiums, and the conditions upon which a borrower can redeem the amount due from him before the expiration of the period for which the advance was made, with tables, where applicable in the opinion of the Registrar, showing the amount due from the borrower after each stipulated payment;
- (f) The manner in which losses are to be ascertained and provided for;

- (g) The manner in which membership is to cease ; and
- (h) Whether the society intends to borrow money, and, if so, within what limits not exceeding those prescribed by the Building Societies Acts.

Annual Accounts.

2.—(1) Every annual account and statement under section forty of the Building Societies Act 1874 shall be made up to the end of the official year of the society to which it relates, and shall be in such form and shall contain such particulars as the Chief Registrar of Friendly Societies may from time to time, with the approval of a Secretary of State, direct, either generally or with respect to any society or class of societies. The form of annual account and statement prescribed for general use by the Chief Registrar under this section, and every alteration of that form, shall, as soon as practicable, be laid before each House of Parliament, and shall not come into operation until the expiration of forty days from the date at which it is so laid. Provided that every such account and statement shall set forth—

- (a) With respect to mortgages to the society upon each of which the present debt does not exceed five thousand pounds (not being mortgages where the repayments are upwards of twelve months in arrear, or where the property has for upwards of twelve months been in possession of the society), the number of all such mortgages, and the aggregate amount owing thereon at the date of the account or statement, such information being given separately in respect of each of the four following classes :—

- (i.) Where the debt does not exceed five hundred pounds :
- (ii.) Where the debt exceeds five hundred pounds and does not exceed one thousand pounds :
- (iii.) Where the debt exceeds one thousand pounds and does not exceed three thousand pounds :
- (iv.) Where the debt exceeds three thousand pounds and does not exceed five thousand pounds ; and
- (b) With respect to any other mortgage to the society, the particulars shown by the appropriate tabular form in the First Schedule to this Act.

(2) Every Auditor, in attesting any such annual account or statement, shall either certify that it is correct, duly vouched, and in accordance with law, or specially report to the society in what respects he finds it incorrect, unvouched, or not in accordance with law, and shall also certify that he has at that audit actually inspected the mortgage deeds and other securities belonging to the society, and shall state the number of properties

with respect to which deeds have been produced to and actually inspected by him.

(3) A copy of every such annual account and statement shall be sent to the Registrar within fourteen days after the annual or other general meeting at which it is presented, or within three months after the expiration of the official year of the society, whichever period expires first.

(4) For the purposes of this section the expression "official year" shall mean, in the case of any society established after the passing of this Act, the year ending with the thirty-first day of December; and, in the case of any society established before the passing of this Act, the year ending with the time up to which its annual account and statement is made at the passing of this Act.

(5) This section shall not come into operation until the expiration of twelve months after the passing of this Act.

Auditors.

3.—Notwithstanding anything in the rules of any society under the Building Societies Acts, one at least of the Auditors of the society shall be a person who publicly carries on the business of an accountant.

Dissolution.

11.—If a society under the Building Societies Acts is dissolved in manner prescribed by its rules or in pursuance of the consent of three-fourths of the members, the liquidators, trustees or other persons having the conduct of the dissolution shall, within twenty-eight days from the termination of the dissolution, send to the Registrar an account and Balance Sheet signed and certified by them as correct, and showing the assets and liabilities of the society at the commencement of the dissolution, and the mode in which those assets and liabilities have been applied and discharged; and in default of so doing shall each be liable to a fine not exceeding five pounds for every day during which the default continues.

Prohibition of Advances.

13.—(1) A society under the Building Societies Acts shall not advance money on the security of any freehold, copyhold, or leasehold estate which is subject to a prior mortgage, unless the prior mortgage is in favour of the society making the advance.

(2) Provided that this section shall not apply to any society in Scotland or Ireland which is at the passing of this Act authorised by the rules to make advances upon second mortgage.

(3) If any advance is made in contravention of this section, the directors of the society who authorised the advance shall be jointly and severally liable for any loss on the advance occasioned to the society.

Borrowing Powers, &c.

14.—In calculating the amount for the time being secured to a society under the Building Societies Acts by mortgages from its members for the purpose of ascertaining the limits of its power to receive deposits or loans at interest, the amount secured on properties the payments in respect of which were upwards of twelve months in arrear at the date of the society's last preceding annual account and statement, and the amount secured on properties of which the society had been twelve months in possession at the date of such account and statement, shall be disregarded.

Provided that this section shall not affect the validity of any deposit or loan which was within the limit provided by law at the time when it was received, and so far as regards any amount secured either on properties the payments in respect of which are upwards of twelve months in arrear at the passing of this Act, or on properties in the possession of the society at the passing of this Act, shall not come into operation until the expiration of three years from the passing of this Act.

15.—(1) A society under the Building Societies Acts shall not use any name or title other than its registered name, and shall not accept any deposit except on the terms that not less than one month's notice may be required by the managers of the society before repayment or withdrawal.

(2) If a society contravenes this section, the society, and also every director or member of the committee of management who is a party to the contravention, shall be liable, on summary conviction, to a fine not exceeding ten pounds, and, in the case of a continuing offence, to an additional fine not exceeding ten pounds for every week during which the offence continues.

16.—(1) A society under the Building Societies Acts may—

- (a) Deposit in a savings bank any money belonging to the society, provided that the whole amount, exclusive of Government stock, credited by the bank to the society does not exceed three hundred pounds at any one time; and
- (b) Invest in Government stock through a savings bank any money of the society, provided that the whole amount of Government stock credited by the bank to the society does not exceed five hundred pounds stock at any one time.

(5) In this section the expressions "savings bank" and "Government stock" have respectively the same meaning as in the Savings Bank Act 1893.

Power of Investment.

17.—The powers of investment under section twenty-five of the Building Societies Act 1874 shall include power to invest in or upon any security in which trustees are for the time being authorised by law to invest.

Penalties.

21.—If any society under the Building Societies Acts neglects or refuses—

- (a) To give any notice, send any return or document, or do or allow to be done anything which the society is by those Acts required to give, send, do or allow to be done; or
- (b) To do any act or furnish any information required for the purposes of those Acts by the Registrar or by an inspector; the society and also every officer thereof bound by the rules thereof to fulfil the duty whereof a breach has been so committed, and if there is no such officer, then every member of the committee of management or board of directors of the society, unless it appears that he was ignorant of or attempted to prevent the breach, shall for each offence be liable, on summary conviction, to a fine not exceeding twenty pounds, and, in the case of a continuing offence, to an additional fine not exceeding five pounds for every week during which the offence continues.

Illicit Bonuses, &c.

23.—No director, secretary, surveyor, solicitor, or other officer of a society under the Building Societies Acts shall, in addition to the remuneration prescribed or authorised by the rules of the society, receive from any other person any gift, bonus, commission, or benefit, for or in connection with any loan made by the society, and any person paying or accepting any such gift, bonus, commission, or benefit, shall be liable, on summary conviction, to a fine not exceeding fifty pounds, and, in default of payment, to be imprisoned with or without hard labour for any time not exceeding six months, and the person accepting any such gift, bonus, commission, or benefit shall, as and when directed by the Court by whom he is convicted, pay over to the

society the amount or value of such gift, bonus, commission, or benefit, and in default of such payment shall be liable to be imprisoned with or without hard labour for any time not exceeding six months.

Application of 1874 Act.

25.—(1) Section forty of the Building Societies Act 1874 shall apply to every society which has been certified under the Building Societies Act 1836 (that is to say, the Act of the session held in the sixth and seventh years of King William the Fourth, chapter 32, intituled “An Act for the regulation of Benefit Building Societies”), and has not been incorporated under the Buildings Societies Act 1874, and exists at the passing of this Act, and if any such society fails to comply with the requirements of that section, the society and its members and officers shall be subject to the like penalties as if the society were a society under the Building Societies Acts.

(2) On the expiration of two years from the passing of this Act, the said Building Societies Act 1836 shall be repealed as to all societies certified thereunder after the year one thousand eight hundred and fifty-six.

Forms.

26.—The forms in the Third Schedule to this Act shall, after the commencement of this Act, be used under the Building Societies Acts.

SCHEDULES.

FIRST SCHEDULE.

PART I.

PARTICULARS to be set forth in the case of a Mortgage where the repayments are not upwards of twelve months in arrear, and the Property has not been upwards of twelve months in possession of the Society, and where the present Debt exceeds £5,000.

1	2	3	4	5	6	7	8	9
Date of Advance	Whether subject to any prior Mortgage or Charge. If so, what amount	Whether Freehold, Copyhold, or Leasehold	Original Valuation of Property	Amount of Advance	Present Debt	Amount of Payments in Advance	Amount of Payments in Arrear	Observations
			£	£	£	£	£	
		Total ..						

PART II.

PARTICULARS to be set forth in the case of Property of which the Society has been upwards of twelve months in Possession.

1	2	3	4	5	6	7	8	9	10	11	12
Roll Numbers	Date of Advance	Date when Possession was taken	Whether subject to any prior Mortgage or Charge. If so, what amount	Whether Freehold, Copyhold, or Leasehold	Amount of Advance	Original Valuation of Property	Debt when Possession was taken	Present Amount included in Assets	Gross Income for the Year	Outgoings for the Year	Observations
					£	£	£	£	£	£	
				Total..							

PART III.

PARTICULARS to be set forth in the case of a Mortgage where the Repayments are upwards of twelve months in arrear and the Property has not been upwards of twelve months in possession of the Society.

1	2	3	4	5	6	7	8	9
Date of Advance	Whether subject to any prior Mortgage or Charge. If so, what amount	Whether Freehold, Copyhold, or Leasehold	Number of Months in Arrear	Original Valuation of Property	Amount of Advance	Present Debt	Amount of Payments in Arrear	Observations
				£	£	£	£	
			Total ..					

SECOND SCHEDULE.

ENACTMENTS REPEALED.

Session and Chapter	Short Title	Extent of Appeal
37 & 38 Vict. c. 42 ..	The Building Societies Act, 1874	Paragraphs 2 and 4 of section sixteen. In sec. 43 the words "in forwarding to the Registrar any returns or information by this Act required or"; the words "or makes a return wilfully false in any respect"; the words "or who shall have made such wilfully false return"; and the words "or false return."
40 & 41 Vict. c. 63 ..	The Building Societies Act, 1877	Sec. 6, and the schedule.

CERTIFICATE OF AUDITORS.

We, the undersigned, _____, being a person who publicly carries on the business of an accountant at No. _____, _____ Street, and _____ residing at _____, the duly appointed Auditors of the above-mentioned Society, do hereby attest the foregoing accounts and statements, and certify that they are correct, duly vouched, and in accordance with law, and we certify that we have, and each of us has, at this audit actually inspected the Mortgage Deeds and other securities belonging to the Society, in respect of each of the Properties in mortgage to the Society referred to in the foregoing accounts and statements.

Signed _____

Signed _____

day of _____ 18 ____.

Presented to the Annual General Meeting of the Society on the _____ day of _____ and adopted.

Signed _____ Chairman.

Countersigned,

Secretary.

FORM OF ANNUAL ACCOUNT AND STATEMENT to be made by a Society under the Building Societies Acts prescribed for general use by the Chief Registrar of Friendly Societies, with the approval of the Secretary of State.

Statement of Accounts of the Building
Society (incorporated 18 and having its registered chief
office or place of meeting at in the County
of) for its th year, ending the
day of 18 .

The number of members of the Society is

I.—RECEIPTS AND PAYMENTS ACCOUNTS.

Dr.

Cr.

To Balance (if any) at Bankers and in hand at beginning of year ..	£ s d	By Balance (if any) due to Bankers at beginning of year ..	£ s d
To Cash received during year, viz. :— [Here are to be stated separately the amounts under each head of receipt]	£ s d	By Cash paid during year, viz. :— [Here are to be stated separately the amounts under each head of payment]	
To Balance (if any) due to Bankers at end of year .. .. .	.. .. .	By Balance (if any) at Bankers and in hand at end of year ..	..

The address to which Rules, Returns, and other documents should be sent is as follows :—

ENGLAND AND WALES : Registry of Friendly Societies, Central Offices, 28 Abingdon Street, Westminster, London, S.W.

SCOTLAND : Registry of Friendly Societies, 43 New Registry House, Edinburgh.

IRELAND : Registry of Friendly Societies, 16 Dame Street, Dublin.

2.—REVENUE (INCLUDING ACCRETIONS TO CAPITAL) AND EXPENDITURE ACCOUNT.

Balances at beginning of Year, as shown by last Annual Statement	Additions during the Year (Stating under each head the total amounts added, and not the excess of additions over diminutions)		Diminutions during the Year (Stating under each head the total diminution, and not the excess of diminution over addition)		Balances at end of Year, as shown by Liabilities and Assets Account.
	Particulars	Amt. £ s d	Particulars	Amt. £ s d	
Due to Shareholders.. ..	Subscriptions of Shareholders: Interest added Other additions, viz.:—	.. .. .. .. .. ..	Withdrawals of Shareholders: Interest paid Other diminutions, viz.:—	.. .. .. .. .. ..	Due to Shareholders (e) ..
Due to Depositors and other Creditors	New Deposits.. .. Interest added Other additions, viz.:—	.. .. .. .. .. ..	Deposits withdrawn Interest paid Other diminutions, viz.:—	.. .. .. .. .. ..	Due to Depositors and other Creditors (f)
Undivided Profit, not includ- ing Prospective Interest ..	Fines and Fees Other sources of Profit, viz.:—	.. .. .. ..	Management expenses, viz.:—	.. ..	Undivided Profit, not includ- ing Prospective Interest (g)
Due on Mortgage Securities, not including Prospective Interest	Advanced on Mortgage Interest due from Borrowers Other additions, viz.:—	.. .. .. .. .. ..	Repayment of Advances Interest received from Bor- rowers Income from Properties in possession Amount written off for Losses Other diminutions, viz.:—	.. .. .. .. .. .. .. .. .. .. .. ..	Due on Mortgage Securities, not including Prospective Interest (h).. ..
Other Assets	Investments made, viz.:—	.. ..	Investments realised, viz.:—	.. ..	Other Assets (i)
Balance deficient (if any) ..	Interest on Investments Other additions, viz.:—	.. .. .. ..	Interest received Other diminutions, viz.:—	.. .. .. ..	Balance deficient (if any) (k)
(A)	(B)	(C)	(D)		
Total .. £	Total .. £	Total .. £	Total .. £		

A and B added together must equal C and D added together.

All the "Totals" must agree.

Cr.

3.—LIABILITIES AND ASSETS ACCOUNT.

Dr.

To Liabilities to Holders of Shares, viz. :—		£ s d	
Principal	Interest	£ s d	
£ s d	£ s d		
[State the liabilities or each class of Shares separately]			
Paid-up Shares
Preferential Shares
Total
(e)			
To Liabilities to Depositors and other Creditors, viz. :—		£ s d	
For Deposits payable at a fixed period ending within the next 12 months	
For Deposits payable at a fixed period ending after the next 12 months	
For Deposits payable upon various times of notice, viz. :—	
Due to Bankers for Loans
To other Creditors for Loans
Other Liabilities, viz. :—
Total
(f)			
To Undivided Profit (including Reserve Funds, but not including Prospective Interest), viz. :—		£ s d	
By Balance Due or Outstanding on Mortgage Securities, not including Prospective Interest, viz. :—		£ s d	
Principal	Interest Accrued (not prospective)	£ s d	
£ s d	£ s d		
Mortgages from Members where the repayments are not upwards of 12 months in arrear, and the property has not been upwards of 12 months in possession of the Society :—			
On — Mortgages where the debt does not exceed £500
On — Mortgages where the debt exceeds £500 and does not exceed £1,000
On — Mortgages where the debt exceeds £1,000 and does not exceed £3,000
On — Mortgages where the debt exceeds £3,000 and does not exceed £5,000
On — Mortgages where the debt exceeds £5,000, as shown by Part I. of the Schedule
Total of Mortgages available under s. 14 of the Act of 1894
[If the Society has any Mortgages from non-members, the like particulars as above are to be given in full for all such Mortgages]			

3.—LIABILITIES AND ASSETS ACCOUNT—(continued).

(g)		(h)	
On — Mortgages on Property of which the Society has been upwards of 12 months in possession, as shown by Part II. of the Schedule		Total	
On — Mortgages where the repayments are upwards of 12 months in arrear, and the property has not been upwards of 12 months in possession of the Society, as shown by Part III. of the Schedule ..			
Total number of properties mortgaged to the Society ..		(i)	
By other Assets:—			
Amount invested in the Funds (bearing interest at — per cent.)			
Amount invested in other securities, viz.:—			
		Nature of Security	Rate of Interest
Other Assets, viz.:—			
Cash at Bankers			
Cash in hands of —			
By Balance deficient (if any)			
(1)		(1)	

(D), (e), (f), (g), (h), (i), (k). These figures must agree with those in the last column of the Revenue and Expenditure Account.

(j). This figure must agree with that in the Certificate of the Auditors.

FRIENDLY SOCIETY ACCOUNTS.

FRIENDLY SOCIETIES ACT, 1875.

38 and 39 Vict. c. 60.

[The whole of this Act is repealed by the Act of 1896 "except in so far as it relates to Societies to which Section 30 applies and to industrial Assurance Societies.

14.—With respect to the duties and obligations of registered societies the following provisions shall have effect :

(1) Every registered society shall—

(f) Once at least in every five years next after the commencement of this Act, or the registry of the society, and so again within six months after the expiration of every five years succeeding the date of the first valuation under this Act, either cause its assets and liabilities to be valued by a valuer to be appointed by the society, and send to the Registrar a report, signed by such valuer, and which shall also state his address and calling or profession, on the condition of the society, and abstract to be made by him of the results of his valuation, together with a return containing such information with respect to the benefits assured and contributions receivable by the society, and of its funds and effects, debts and credits, as the Registrar may from time to time require, or send to the Registrar a return of the benefits assured and contributions receivable from all the members of the society, and of all its funds and effects, debts and credits, accompanied by such evidence in support thereof as the Chief Registrar prescribes, in which case the Registrar shall cause the assets and liabilities of the society to be valued and reported on by some actuary, and shall send to the society a copy of his report, and an abstract of the results of his valuation :

(g) Allow any member or person having an interest in the funds of the society to inspect the books at all reasonable hours at the registered office of the society, or at any place where the same are kept, except that no such member or person, unless he be an officer of the society, or be specially authorised by a resolution of the society to do so, shall have the right to inspect the Loan Account of any other member without the written consent of such member.

30.—(8) A copy of every Balance Sheet of a society shall, during the seven days next preceding the meeting at which the same is to be presented, be kept open by the society for inspection at every office at which the business of the society is carried on, and shall be delivered or sent prepaid to every member on demand.

(9) The annual returns shall be certified by some person not an officer of the society (otherwise than as Auditor thereof) carrying on publicly the business of an accountant, and if not so certified shall be deemed not to have been made.

35.—The Treasury may from time to time appoint public Auditors and valuers for the purposes of this Act, and may determine from time to time the rates of remuneration to be paid by societies for the services of such Auditors and valuers; but the employment of such Auditors and valuers is not compulsory on any society.

36.—The Treasury may determine a scale of fees to be paid for matters to be transacted or for the inspection of documents under this Act; but no fees shall be payable on the registry of any friendly, benevolent, or cattle insurance society, or working men's club, or of any amendment of the rules of the same.

All fees which may be received by any Registrar under, or by virtue of, this Act shall be paid into the receipt of Her Majesty's Exchequer.

37.—The Treasury shall, out of money to be provided by Parliament, pay to the Chief and Assistant Registrars such salaries or other remunerations respectively, and such sums of money for defraying the expenses of office rent, salaries of assistants, clerks, and servants, remuneration of actuaries, accountants, and inspectors, computation of tables, publication of documents, diffusion of information, expenses of prosecutions, travelling expenses, and other allowances of the Chief or any Assistant Registrar, and other expenses which may be incurred for carrying out the purposes of this Act, and may also pay to any public Auditors or valuers to be appointed under this Act such remuneration (if any) as the Treasury shall from time to time allow.

Schedule 2 states that the rules of societies registered under this Act must contain clauses to the following effect:—

(1) The keeping separate accounts of all moneys received or paid on account of every particular fund or benefit assured for which a separate table of contributions payable shall have been adopted, and the keeping separate account of the expenses of management, and of all contributions on account thereof.

(5) The investment of the funds, the keeping of the accounts, and the audit of the same once a year at least.

(6) Annual returns to the Registrar of the receipts, funds, effects, and expenditure and numbers of members of the society.

(7) The inspection of the books of the society by every person having an interest in the funds of the society.

FRIENDLY SOCIETIES ACT, 1896.

59 and 60 Vict. c. 25.

Appointment of Trustees.

25.—(1) Every registered society and branch shall have one or more trustees.

(4) The same person shall not be secretary or treasurer of a registered society or branch and a trustee of that society or branch.

Audit.

26.—(1) Every registered society and branch shall once at least in every year submit its accounts for audit either to one of the public Auditors appointed as in this Act mentioned, or to two or more persons appointed as the rules of the society or branch provide.

(2) The Auditors shall have access to all the books and accounts of the society or branch, and shall examine the annual return mentioned in this Act, and verify the annual return with the accounts and vouchers relating thereto, and shall either sign the annual return as found by them to be correct, duly vouched, and in accordance with law, or specially report to the society or branch in what respects they find it incorrect, unvouched, or not in accordance with law.

Annual Returns.

27.—(1) Every registered society and branch shall once in every year, not later than the 31st day of May, send to the Registrar a return (in this Act called the annual return) of the receipts and expenditure, funds, and effects of the society or branch as audited.

(2) The annual return must—

(a) show separately the expenditure in respect of the several objects of the society or branch; and

(b) be made out to the 31st day of December then last inclusively; and

- (c) state whether the audit has been conducted by a public Auditor appointed as by this Act provided, and by whom, and, if by persons other than a public Auditor, state the name, address, and calling or profession of every such person, and the manner in which, and the authority under which, he is appointed.

(3) The society or branch shall, together with the annual return, send a copy of the special report of the Auditors.

(4) In the case of a branch the annual return shall be sent to the Registrar through an officer appointed in that behalf by the society of which the branch forms part.

Quinquennial Valuation.

28.—(1) Every registered society and branch shall, except as in this section provided, once at least in every five years either—

- (a) cause its assets and liabilities to be valued by a valuer to be appointed by the society or branch and send to the Registrar a report on the condition of the society or branch; or
- (b) send to the Registrar a return of the benefits assured and contributions receivable from all the members of the society or branch, and of all its funds and effects, debts and credits, accompanied by such evidence in support thereof as the Chief Registrar prescribes.

(2) If the society or branch sends to the Registrar such report as aforesaid, the report must—

- (a) be signed by the valuer; and
- (b) state the address and calling or profession of the valuer; and
- (c) contain an abstract to be made by the valuer of the results of his valuation, together with a statement containing such information with respect to the benefits assured and the contributions receivable by the society or branch, and of its funds and effects, debts and credits, as the Registrar may require.

(3) If the society or branch sends to the Registrar such return as aforesaid, he shall cause the assets and liabilities of the society or branch to be valued and reported on by some actuary, and shall send to the society or branch a copy of the report and an abstract of the results of the valuation.

(4) Provided that this section shall not apply to—

- (a) a benevolent society, working men's club, cattle insurance society or branch thereof; or

(b) a specially authorised society or branch unless it is so directed in the authority for registering that society or branch.

(5) Provided also that the Chief Registrar may, with the approval of the Treasury, dispense with the provisions of this section in respect of societies or branches to whose purposes or to the nature of whose operations he may deem those provisions inapplicable.

Balance Sheet.

29.—Every registered society and branch shall keep a copy of the last annual Balance Sheet, and of the last quinquennial valuation, together with any special report of the Auditors, always hung up in a conspicuous place at the registered office of the society or branch.

Public Auditors and Valuers.

30.—(1) For the purpose of audits and valuations to be made under this Act the Treasury may appoint public Auditors and valuers and may determine the rates of remuneration to be paid by societies and branches for the services of those Auditors and valuers; but the employment of those Auditors and valuers shall not be compulsory.

(2) The Treasury may, out of money to be provided by Parliament, pay to the public Auditors and valuers such remuneration (if any) as the Treasury may allow.

Exemptions from Stamp Duty.

33.—Stamp duty shall not be chargeable upon any of the following documents:—

- (a) Draft or order or receipt given by or to a registered society or branch in respect of money payable by virtue of its rules or of this Act.
- (b) Letter or power of attorney granted by any person as trustee for the transfer of any money of a registered society or branch invested in his name in the public funds.
- (c) Bond given to or on account of a registered society or branch or by the treasurer or other officer thereof.
- (d) Policy of insurance or appointment or revocation of appointment of agent or other document required or authorised by this Act or by the rules of a registered society or branch.

Rights of Members, &c.

39.—Every registered society and branch shall supply gratuitously to every member or person interested in its funds, on his application, either

- (a) a copy of the last annual return of the society or branch; or
- (b) a Balance Sheet or other document duly audited containing the same particulars as to the receipts and expenditure, funds and effects, of the society or branch as are contained in the annual return.

40.—A member or person having an interest in the funds of a registered society or branch may inspect the books at all reasonable hours at the registered office of the society or branch, or at any place where the books are kept, except that the member or person shall not, unless he is an officer of the society or branch, or is specially authorised by a resolution of the society or branch to do so, have the right to inspect the loan account of any other member without the written consent of that member.

41.—(1) A member, or person claiming through a member of a registered friendly society or branch, shall not be entitled to receive more than two hundred pounds by way of gross sum, together with any bonuses or additions declared upon assurances not exceeding that amount, or (except as provided by this Act) fifty pounds a year by way of annuity, from any one or more such societies or branches.

(2) Any such society or branch may require a member, or person claiming through a member, to make and sign a statutory declaration that the total amount to which that member or person is entitled from one or more such societies or branches does not exceed the sums aforesaid.

42.—The rules of a registered society or branch may provide for accumulating at interest, for the use of any member, any surplus of his contributions to the funds of the society or branch which may remain after providing for any assurance in respect of which they are paid and for the withdrawal of the accumulations.

Property, Funds, and Investments.

44.—(1) The trustees of a registered society or branch may, with the consent of the committee or of a majority of the members present and entitled to vote in general meeting, invest the funds of the society or branch or any part thereof, to any amount in any of the following ways:—

- (a) In the Post Office Savings Bank, or in any savings bank certified under the Trustee Savings Banks Act 1863; or
- (b) In the public funds; or
- (c) With the National Debt Commissioners as in this Act provided; or
- (d) In the purchase of land, or in the erection or alteration of offices or other buildings thereon; or
- (e) Upon any other security expressly directed by the rules of the society or branch, not being personal security, except as in this Act authorised with respect to loans.

(2) The rules of a society with branches and of any branch thereof may provide for the investment of funds of the society or of that branch by the trustees of any branch, or by the trustees of the society, and the consent required for any such investment shall be the consent of the committee, or of such majority as aforesaid of the society or branch by whom the funds are invested.

45.—(1) A registered society and, subject to the rules of the society, a registered branch may advance to a member of at least one full year's standing any sum not exceeding one-half of the amount of an assurance on his life, on the written security of himself, and two satisfactory sureties for repayment.

(2) The amount so advanced, with all interest thereon, may be deducted from the sum assured, without prejudice in the meantime to the operation of the security.

46.—A registered society may, out of any separate loan fund to be formed by contributions or deposits of its members, make loans to members on their personal security, with or without sureties, as may be provided by the rules, subject to the following restrictions:—

- (a) A loan shall not at any time be made out of money contributed for the other purposes of the society:
- (b) A member shall not be capable of holding any interest in the loan fund exceeding two hundred pounds:
- (c) A society shall not make any loan to a member on personal security beyond the amount fixed by the rules, or make any loan which, together with any money owing by a member to the society, exceeds fifty pounds:
- (d) A society shall not hold at any one time on deposit from its members any money beyond the amount fixed by the rules, and the amount so fixed shall not exceed two-thirds of the total sums owing to the society by the members who have borrowed from the loan fund.

47.—(1) A registered society or branch may (if the rules thereof so provide) hold, purchase, or take on lease in the names of the trustees of the society or branch any land, and may sell, exchange, mortgage, lease, or build upon that land (with power to alter and pull down buildings and again rebuild), and a purchaser, assignee, mortgagee, or tenant shall not be bound to inquire as to the authority for any sale, exchange, mortgage, or lease by the trustees, and the receipt of the trustees shall be a discharge for all sums of money arising from or in connection with the sale, exchange, mortgage, or lease.

(2) A branch of a registered society need not for the purposes of this section be separately registered.

(3) Nothing in this section shall authorise a benevolent society to hold land exceeding one acre in extent.

48.—Where a registered society or branch is entitled in equity to any hereditaments of copyhold or customary tenure, either absolutely or by way of mortgage or security, the lord of the manor of which the hereditaments are held shall, if the society or branch so requires, admit not more than three trustees of the society or branch as tenants in respect of such hereditaments, on payment of the usual fines, fees, and other dues payable on the admission of a single tenant.

49.—(1) All property belonging to a registered society, whether acquired before or after the society is registered, shall vest in the trustees for the time being of the society, for the use and benefit of the society, and the members thereof, and of all persons claiming through the members according to the rules of the society.

(2) The property of a registered branch of a society shall vest wholly or partly in the trustees for the time being of that branch or of any other branch of which that branch forms part (or, if the rules of the society so provide, in the trustees for the time being of the society), for the use and benefit either of the members of any such branch and persons claiming through those members, or of the members of the society generally, and persons claiming through them, according to the rules of the society.

(3) The trustees shall not be liable to make good any deficiency in the funds of the society or branch, but shall be liable only for sums of money actually received by them respectively on account of the society or branch.

50.—Upon the death, resignation, or removal of a trustee of a registered society or branch, the property vested in that trustee shall, with-

out conveyance or assignment, and whether the property is real or personal, vest, as personal estate subject to the same trusts, in the succeeding trustees of that society or branch either solely or together with any surviving or continuing trustees, and, until the appointment of succeeding trustees, shall so vest in the surviving or continuing trustees only, or in the executors or administrators of the last surviving or continuing trustee, except that stocks and securities in the public funds of Great Britain and Ireland shall be transferred into the names of the succeeding trustees, either solely or jointly with any surviving or continuing trustees.

51.—In all legal proceedings whatsoever concerning any property vested in the trustees of a registered society or branch, the property may be stated to be the property of the trustees in their proper names as trustees for the society or branch without further description.

52.—(1) A registered society or branch may pay to the account of the National Debt Commissioners at the Bank of England or the Bank of Ireland, as the case may require, any sum of money not less than fifty pounds upon a declaration of the trustees of the society or branch or any two of them, that the money belongs exclusively to the society or branch.

(2) The cashier of the bank shall receive all such sums of money and place them to the account of the Commissioners in the book of the bank named "The Fund for Friendly Societies."

(3) A sum of money paid in upon a false declaration shall be forfeited to the Commissioners, and applied by them in the manner directed by Section 12 of the Savings Banks Act 1891.

(4) The provisions of Sections 21, 22, 24, 25, 26, 27, and 28 of the Trustee Savings Banks Act 1863, as to the regulation of receipts, certificates, and orders, shall apply to money paid under this section.

(5) A society or branch so investing money with the Commissioners shall be entitled to a receipt entitling to interest at the following rates:—

To a friendly society or branch legally established before the twenty-eighth of July one thousand eight hundred and twenty-eight, which has invested funds with the Commissioners before the twenty-third of July one thousand eight hundred and fifty-five, a rate of interest in respect of any assurance made before the fifteenth of August one thousand eight hundred and fifty of . . .

Three pence per
centum per diem.

To a friendly society or branch legally established between the twenty-eighth of July one thousand eight hundred and twenty-eight and the fifteenth of August one thousand eight hundred and fifty, which had invested funds with the Commissioners before the twenty-third of July one thousand eight hundred and fifty-five, a rate of interest in respect of any assurance made before the fifteenth of August one thousand eight hundred and fifty of

Twopence half-penny per centum per diem.

To a friendly society or branch legally established before the twenty-eighth of June one thousand eight hundred and eighty-eight, which had invested funds with the Commissioners before the first day of January one thousand eight hundred and ninety-six a rate of interest in respect of any assurance made on or before the said twenty-eighth day of June of

Twopence per centum per diem.

To a society or branch in respect of any investment with the Commissioners, other than as hereinbefore in this section mentioned, a rate of interest of.. .. .

Two pounds fifteen shillings per centum per annum.

(6) A society or branch withdrawing money so invested with the Commissioners shall not be entitled to make any further deposit without their consent.

(7) A society or branch so investing money with the Commissioners shall furnish such returns as may be required by the Commissioners, in respect of the funds deposited with them, and the assurances to which those funds relate.

(8) A society or branch having funds invested with the Commissioners at a rate higher than two pounds fifteen shillings per centum per annum shall retain at that rate so much only of its funds as arises from assurances made before the date applicable to that rate, after deducting all benefit payments and management expenses incurred on account of those assurances; and whenever the society or branch fails to satisfy the Commissioners of its title to retain at that rate any part of its funds, the Commissioners shall require the withdrawal thereof,

or the transfer thereof to the rate of twopence per centum per diem, or two pounds fifteen shillings per centum per annum, as the case may require, and in default of withdrawal within thirty days, shall transfer the same in their books accordingly, and shall notify the transfer to the society or branch.

(9) Whenever it appears to the Commissioners that all the members of a society or branch assured before the fifteenth day of August one thousand eight hundred and fifty have died or ceased to be members, the Commissioners shall forthwith transfer in their books to the rate of twopence per centum per diem, or two pounds fifteen shillings per centum per annum, as the case may require, all funds of the society or branch remaining invested at any higher rate, and shall notify the transfer to the society or branch.

53.—(1) A receipt under the hands of the trustees of a registered society or branch, countersigned by the secretary, for all sums of money secured to the society or branch by any mortgage or other assurance, being in the form prescribed by this Act, if endorsed upon or annexed to the mortgage or other assurance, shall vacate the mortgage or assurance and vest the property therein comprised in the person entitled to the equity of redemption of that property, without re-conveyance or re-surrender.

(2) If the mortgage or other assurance has been registered under any Act for the registration or record of deeds or titles, or is of copyholds or of lands of customary tenure and entered on any Court rolls, the Registrar under any such Act, or recording officer, or steward of the manor, or keeper of the register, shall, on production of the receipt, verified by oath of any person, enter satisfaction of the mortgage or charge made by the assurance on the register or Court rolls, and shall grant a certificate, either upon the mortgage or assurance, or separately to the like effect.

(3) The certificate shall be received in evidence in all Courts and proceedings without further proof.

(4) The person making the entry shall be entitled for making the said entry and granting the said certificate to a fee of two shillings and sixpence, which in Ireland shall be paid by stamps and applied in accordance with the Public Offices Fees Act, 1879.

(5) This section shall not extend to Scotland or the Island of Jersey.

Officers in Receipt or Charge of Money.

54.—Every officer of a registered society or branch having receipt or charge of money shall, if the rules of the society or branch so require,

before taking upon himself the execution of his office, become bound with one sufficient surety at the least in a bond or give the security of a guarantee society, in such sum as the society or branch directs, conditioned for his rendering a just and true account of all sums of money received and paid by him on account of the society or branch at such times as its rules appoint, or as the society or branch or the trustees or committee thereof require him to do, and for the payment by him of all sums due from him to the society or branch.

55.—(1) Every officer of a registered society or branch having receipt or charge of money shall, at such times as by the rules of the society or branch he should render account, or upon demand made, or notice in writing given or left at his last or usual place of residence, give in his account as may be required by the society or branch, or by the trustees or committee thereof, to be examined and allowed or disallowed by them, and shall, on the like demand or notice, pay over all sums of money and deliver all property in his hands or custody to such person as the society or branch, or the committee or the trustees, appoint.

(2) In case of any neglect or refusal to deliver the account, or to pay over the sums of money or to deliver the property in manner aforesaid, the trustees or authorised officers of the society or branch may sue upon the bond or security before mentioned, or may apply to the County Court or to a Court of summary jurisdiction, and the order of either such Court shall be final and conclusive.

Offences, Penalties, and Legal Proceedings.

88.—If any person wilfully makes, orders, or allows to be made any entry, erasure in, or omission from a Balance Sheet of a registered society or branch, or a return or document required to be sent, produced, or delivered for the purposes of this Act, with intent to falsify the same, or to evade any of the provisions of this Act, he shall be liable to a fine not exceeding fifty pounds.

Application of Act.

101.—(1) This Act shall apply to societies and branches subsisting at the commencement of this Act, which, or the rules of which, have been registered, enrolled, or certified under any Act relating to friendly societies or cattle insurance societies, as if they had been registered under this Act, and the rules of those societies and branches shall, so far as they are not contrary to any express provision of this Act, continue in force until altered or rescinded.

(2) Where the contingent annual payments to which the members or he nominees of the members of friendly societies or branches, estab-

lished before the fifteenth day of August one thousand eight hundred and fifty, may become entitled exceed the limit fixed by this Act, the rules of those societies and branches shall continue to be valid, anything in this Act to the contrary notwithstanding.

102.—In the application of this Act to Scotland :—

The expression “land” shall include heritable subjects of whatever description ;

The expressions “Court of summary jurisdiction” and “County Court” shall mean the Sheriff Court of the county ;

The expression “administration” shall mean confirmation ;

The expression “misdemeanour” shall mean crime and offence.

SCHEDULES.

THE FIRST SCHEDULE.

Matters to be provided for by the Rules of Societies Registered under this Act.

1. The name and place of office of the society.
2. The whole of the objects for which the society is to be established, the purposes for which the funds thereof shall be applicable, the terms of admission of members, the conditions under which any member may become entitled to any benefit assured thereby, and the fines and forfeitures to be imposed on any member, and the consequences of non-payment of any subscription or fine.
3. The mode of holding meetings and right of voting, and the manner of making, altering, or rescinding rules.
4. The appointment and removal of a committee of management (by whatever name), of a treasurer and other officers, and of trustees, and in the case of a society with branches the composition and powers of the central body, and the conditions under which a branch may secede from the society.
5. The investment of the funds, the keeping of the accounts, and the audit of the same once a year at least.
6. Annual returns to the Registrar of the receipts, funds, effects, and expenditure, and number of members of the society.

7. The inspection of the books of the society by every person having an interest in the funds of the society.

8. The manner in which disputes shall be settled.

9. In case of dividing societies, a provision for meeting all claims upon the society existing at the time of division before any such division takes place.

And also in the case of friendly and cattle insurance societies.

10. The keeping separate accounts of all moneys received or paid on account of every particular fund or benefit assured for which a separate table of contributions payable shall have been adopted, and the keeping separate account of the expenses of management, and of all contributions on account thereof.

11. (Except as to cattle insurance societies) a valuation once at least in every five years of the assets and liabilities of the society, including the estimated risks and contributions.

12. The voluntary dissolution of the society by consent in a friendly society of not less than five-sixths in value of the members, and of every person for the time being entitled to any benefit from the funds of the society, unless his claim be first satisfied or adequately provided for; and in a cattle insurance society by consent of three-fourths in numbers of the members.

13. The right of one-fifth of the total number of members, or of one hundred members in the case of a society of one thousand members and not exceeding ten thousand, or of five hundred members in the case of a society of more than ten thousand members, to apply to the Chief Registrar, or in the case of societies registered and doing business exclusively in Scotland or Ireland to the Assistant Registrar for Scotland or Ireland, for an investigation of the affairs of the society, or for winding up the same.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR.

The principal points to be attended to in filling up the Return are:—

1. Receipts and Expenditure. It must be carefully remembered that this is not a mere Cash Account, giving particulars of cash received and cash expended. Accordingly, such items as—

(a) Cash withdrawn from bank or cash paid into bank,

(b) Cash expended in purchase of investments, or cash received on sale of investments, or on discharge of mortgages, &c. &c., must not appear beyond entering as a profit or loss, as the case may be, the difference between the amount received and the amount at which the asset previously stood in the society's Balance Sheet.

2. Interest on the funds which have become due and payable in the course of the year should appear as a receipt, and if not actually paid at end of year will appear in the assets of the Balance Sheet as interest due and unpaid.

3. Where under the rule separate funds are required to be kept for the various benefits, the amounts of these various funds should always be stated separately in the Balance Sheet (Form B), *the total amount of funds agreeing with that stated under Receipts and Expenditure Account.*

4. Where any particular fund has no assets, but is indebted for the time being to other funds, the amount of such indebtedness, clearly described, must appear under "Other assets," and when a deficiency in any fund exists, both at the beginning and end of the year, the amount of such deficiency at the beginning of the year must be stated below the item "Amount of funds at end of the year, as per Balance Sheet," and the amount of such deficiency at the end of the year below the item "Amount of funds at the beginning of the year," in each case being clearly described.

5. The amount of benefit (or management) fund (or funds) brought forward at beginning of year must agree with corresponding amounts at close of the previous year.

6. Whatever the rules may provide as to date of annual meeting and annual accounts, the annual return required under the Act to be made and sent to the Registrar must always be made up for the year ending 31st December.

7. The amount of contributions received in the course of the year in respect of any particular fund should be so entered as to include contributions remaining unpaid at 31st December, but not in arrear to the extent of forfeiture of membership, and this latter should appear as "contributions in arrear" among the assets of the Balance Sheet, and would consequently not be included in the item "contributions" for the next year.

8. Unless the Auditor is one of the public Auditors appointed by the Lords of the Treasury under the Act, the annual return must be signed by at least two Auditors appointed under the society's rules, as well as by the officers specified.

9. That each account be correctly added up.
10. The totals at the bottom, on the opposite sides of each account, to be the same.
11. That the funds of the society are invested in strict accordance with the registered rules of the society. The investment of moneys on notes of hand and other personal securities is not legal.
12. That all receipts and expenditure outside the objects of the society, such as for banners, fêtes, anniversaries, &c., be not included in the return.

Societies are reminded that the valuations under the Act must be sent to the Registrar once at least in every five years. (See Section 14 (1) (f) of the 38 & 39 Vict. c. 60.)

[Fill up the blank lines with Name, Registered Office, and Registered
Number of the Society.]

Name of Society _____

Registered Office of Society _____

in the County of _____ Register No. _____

Received a document purporting to be the Annual Return of the Society
for the year 1894.

N.B.—On receipt with the return of an envelope of sufficient size, written on the top "*On His Majesty's Service*," directed as the society may desire, the above acknowledgment (which is not to be taken as implying that a valid return has been received) will be forwarded.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—*continued*.

FORMS A AND B.

RETURN REQUIRED FROM A REGISTERED SOCIETY.

(Not being a collecting Society within s. 30 of the Act.)

Year ending 31st December 1894.

[The Society's Balance Sheet cannot be accepted as a substitute for this Return.]

This Return is to be sent to the Registrar before the 1st of June 1895.

A copy of the Auditor's Report, if any, should also be sent.

Name of Society

Register No.

Date of Commencement of Society 18 .

When first Enrolled, Certified, or Registered

Names of the present Trustees

Name and address of the Treasurer and of any
other Officer in receipt or charge of money)Amount of Security given by him or them £

Number of benefit members at the beginning of the year ..

Number of benefit members admitted during the year ..

Together

Number of benefit members who died during the year }

Number of benefit members who left from other causes }

Total number of benefit members at the end of the year ..

Average amount of Funds per member (that is, the total funds
on the 31st December 1894, divided by the total number of
benefit members) £

State what provision, if any, is made for old age

The Audit for the year has been conducted by Mr. , Public

Auditor,* [or by of

whose calling or profession is , and

of , whose calling or profession

is , who were appointed Auditors by

under the authority of Rule No.].

Registered Office of the Society† in the county of

Date 1895.

* This term means only a Public Auditor appointed under the Friendly Societies Acts.

† State full postal address.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—FORM A—continued.

MANAGEMENT FUND.*

RECEIPTS.

EXPENDITURE.

	£ s d		£ s d		(b) Specify their nature
	£	s d	£	s d	
Donations of Honorary Members to this Fund	Salaries .. ..	..	..
Contributions of Members for Management	Rent .. ..	..	..
Levies upon Members for Management	Printing, Stationery, and Postage .. ..	..	..
Entrance Fees	Other Payments (if any) (b) .. ..	..	..
Fines appropriated to this Fund by the Society's Rules			
Interest on Investments of Management Fund	Total Expenses of Management .. ..	..	..
Other Receipts (if any) (b)	Bad Debts and Losses .. ..	..	..
			Cost of Medical Aid .. ..	..	..
Contributions for Medical Aid			
			Total Expenditure .. ..	..	..
Total Receipts	Amount of Management Fund at the end of the year, as per Balance Sheet (below) .. ..	..	..
Amount of Management Fund at the beginning of the year	Total	£	
Total	£				

* If the Society was registered before 23rd July 1855, and has no separate Management Fund provided for in its rules, state the fact.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—FORM A—*continued*.

Dr.

BALANCE SHEET OF FUNDS AND EFFECTS

Cr.

	£	s	d		£	s	d
	INVESTMENTS :						
	1. In the interest at Savings Bank, yielding per cent.						
	2. In the Public Funds (i)						
	3. With the Commissioners for the Reduction of the National Debt, yielding interest at per cent						
	4. Upon Government Securities in Great Britain or Ireland, yielding interest at per cent.						
	5. Upon Real Securities in Great Britain or Ireland, yielding interest at an average of per cent.						
	6. In the Purchase of Land						
	7. In the Erection of Offices and Buildings						
	8. In (k)						
	Cash in the Post Office Savings Bank						
	Cash in hand (l)						
	Other Assets (if any) (m)						
	Total						
	Total						

	Amount of Benefit Fund (as above)	£	s	d
	Amount of Management Fund (as above)			
(c) Specify their nature	Debts (if any) legally incurred by Trustees on behalf of the Society (c)			
	Cash due to Treasurer (if any)			
(d) Specify them	Other Liabilities (d)			
	Total	£	s	d

* Give Postal Address.

residing at *

Signature of Secretary

Signature of Treasurer or one of the Trustees

The undersigned, having had access to all the Books and Accounts of the Society, and having examined the foregoing General Statement, and verified the same with the Accounts and Vouchers relating thereto, now sign the same as found to be correct, duly vouched, and in accordance with law.

* Public Auditor : or _____ and _____ Auditors. Date _____ 1895.

* This term means only a Public Auditor appointed under the Friendly Societies Act.

If in any respect these Accounts are incorrect, unvouched, or not in accordance with law, the Auditors are not to sign as above, but are to make a special report to the Society, of which a copy is to be sent to the Registrar with this Statement

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—*continued.*

EXTRACTS FROM 38 AND 39 VICT. C. 60.

Duties and Obligations of Societies.

14.—With respect to the duties and obligations of registered societies the following provisions shall have effect:—

(1) Every registered society shall—

Audit.

- (c) Once at least in every year submit its accounts for audit either to *one of the public Auditors* appointed as herein mentioned, or to *two or more persons appointed as the rules of the society provide*, which Auditors shall have access to all the books and accounts of the society, and shall examine the general statement of the receipts and expenditure, funds and effects of the society, and verify the same with the accounts and vouchers relating thereto, and shall either sign the same as found by them to be correct, duly vouched, and in accordance with law, or specially report to the society in what respects they find it incorrect, unvouched, or not in accordance with law.

Annual Returns.

- (d) Once in every year before the first day of June send to the Registrar a general statement (to be called the annual return) of the receipts and expenditure, funds and effects of the society *as audited*, which shall show separately the expenditure in respect of the several objects of the society, and shall be made out to the thirty-first December then last inclusively, and a copy of the Auditor's report, if any, shall also be sent to the Registrar with such general statement; and such annual return shall state whether the audit has been conducted by a public Auditor appointed as in this Act provided, and by whom; and, if by any person or persons other than a public Auditor, shall state the name, address, and calling or profession of each of such persons, and the manner in which, and the authority under which, they were respectively appointed.

Supplying Copies of Annual Returns.

- (h) Supply gratuitously every member or person interested in the funds of the society, on his application, with a copy of the last annual return of the society for the time being. Provided that it shall

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—*continued*.

be deemed a sufficient compliance with this requirement if the society supplies gratuitously every member or person interested with a Balance Sheet or other document duly audited, containing the same particulars as to the receipts and expenditure, funds and effects of the society as are contained in the annual return.

- (i) Keep a copy of the last annual Balance Sheet for the time being and of the last quinquennial valuation for the time being, together with the report of the Auditors, if any, always hung up in a conspicuous place at the registered office of the society.

Offences.

(3) It shall be an offence under this Act if any registered society or any officer or member thereof—

- (a) *Fails to give any notice, send any return or document, or do or allow to be done, any act or thing which the society, officer, or person is by this Act required to give, send, do, or allow to be done.*
- (b) *Wilfully neglects or refuses to do any act, or to furnish any information required for the purposes of this Act by the Chief or any other Registrar, or other person authorised under this Act, or does any act or thing forbidden by this Act.*
- (c) *Makes a return, or wilfully furnishes any information, in any respect false or insufficient.*

Offence by Societies to be also Offences by Officers, &c.

(4) Every offence by a society under this Act shall be deemed to have been also committed by every officer of the same bound by the rules thereof to fulfil any duty whereof such offence is a breach, or if there be no such officer, then by every member of the committee of management of the same, unless such member be proved to have been ignorant of or to have attempted to prevent the commission of such offence; and every default under this Act constituting an offence if continued, constitutes a new offence in every week during which the same continues.

Returns to be in Prescribed Form.

(5) Every *annual or other return*, abstract of valuation, and other document required for the purposes of this Act, *shall be made in such form, and shall contain such particulars, as the Chief Registrar prescribes.*

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—*continued*.

Penalties.

32.—With respect to penalties under this Act, the following provisions shall have effect :—

Penalty for Falsification.

(1) If any person wilfully makes, orders, or allows to be made, any entry, erasure in, or omission from any Balance Sheet of a registered society, or any contribution or collecting book, or any return or document required to be sent, produced, or delivered for the purposes of this Act, with intent to falsify the same, or to evade any of the provisions of this Act, he is liable to a penalty not exceeding fifty pounds, recoverable at the suit of the Chief or any Assistant Registrar, or of any person aggrieved.

Penalties for Ordinary Offences.

(2) Every society, officer, or member of a society, or other person guilty of an offence under this Act for which no penalty is expressly provided herein is liable to a penalty of *not less than one pound*, and not more than five pounds, recoverable at the suit of the Chief or any Assistant Registrar, or of any person aggrieved.

Recovery of Penalties.

(3) All penalties imposed by this Act, or to be imposed by any regulations under the same, or by the rules of a registered society, are recoverable in a Court of summary jurisdiction.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR.—*continued.**N.B.—Societies to which this Form applies need not fill up Form A.*

FORM B.—For Societies whose members pay more than one contribution for Benefits.

RECEIPTS.

BENEFIT FUNDS.

EXPENDITURE.

	£ s d		£ s d		£ s d	
	£	s	£	s	£	s
(a) Where levies are made for benefits, in addition to the contributions and levies for each benefit should be separately stated. Where a single contribution provides for more than one benefit, the lines may be bracketed together.						
(b) If under more than one Table, the amount under each Table should be separately stated.						
(c) Other benefits (if any) for which separate contributions are paid should be stated separately.						
d) Specify their nature.						
Entrance Fees (not appropriated to Management Fund)						
Contributions (a) for Sickness (b)						
Contributions for suns at Death (b)						
Contributions for Annuities						
Contributions for Endowments						
Contributions for Old Age Pay [where separate]						
Contributions for Widows and Orphans' Allowances [where separate]						
Contributions for Lying-in [where separate]						
Contributions for Accidents [where separate]						
Contributions for Travelling Benefit [where separate]						
Contributions for Distress Relief [where separate]						
Contributions for Medical Aid [where separate]						
Contributions to separate Loan Fund [under s. 18 (2) of Act]						
Contributions for (c)						
Contributions for						
Contributions for						
Fines not appropriated to Management Fund						
Interest on Investments of Benefit Funds						
Other Receipts (if any) (d)						
Total Receipts						
Amount of Benefit Funds at the beginning of the year						
Total						
Weeks pay to members on full pay (lasted by rules weeks)						
Weeks pay to members on reduced pay (last period lasting weeks)						
Weeks pay to members on reduced pay (and period lasting weeks) (h)						
(i) members and children of members above to years of age						
(j) wives [or husbands] of members of children under 5 years of age						
(k) of children between 5 and 10 years of age						
Sum at Death						
Annuities						
Endowments						
Old Age Pay						
Widows and Orphans' Allowances						
Lying-in Pay						
Accident Allowances						
Travelling Benefit						
Distress Relief						
Cost of Medical Aid (if paid out of a separate fund)						
Loans out of separate Loan Fund [under s. 18 (2) of Act] (This amount must not be included in total expenditure.)						
Payments for other Benefits (if any) (i)						
Other Payments (if any) (k)						
Total Expenditure						
Amount of Benefit Funds at the end of the year, as per Balance Sheet (below)						
Total						

(h) If any further reductions, they should be stated separately.

(i) State separately the expenditure for each.
(k) Specify their nature.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—FORM B—*continued*.

MANAGEMENT FUND.*

RECEIPTS.

EXPENDITURE.

	£ s d			£ s d			(d) Specifying their nature.
	£	s	d	£	s	d	
Donations of Honorary Members appropriated to this Fund	Salaries	(d) Specifying their nature.
Contributions of Members for Management	Rent .. .. .	..	..
Levies upon Members for Management	Printing, Stationery, and Postages .. .. .	..	..
Entrance Fees	Other Payments (if any) (d) .. .. .	..	..
Fines appropriated to this Fund by the Society's Rules	Total Expenses of Management .. .. .	..	..
Interest on Investments of Management Fund	Bad Debts and Losses..	(d) Specifying their nature.
Other Receipts (if any) (d)	Cost of Medical Aid .. .. .	..	..
Contributions for Medical Aid	Total Expenditure .. .. .	..	..
Total Receipts	Amount of Management Fund at the end of the year as per Balance Sheet (below) .. .. .	..	..
Amount of Management Fund at the beginning of the year	Total .. .. .	..	..
Total		£		

* If the Society was registered before 23rd July 1855, and has no separate Management Fund provided for in its rules, state the fact.

ANNUAL RETURN AS PRESCRIBED BY THE CHIEF REGISTRAR—FORM B—*continued*.
BALANCE SHEET OF FUNDS AND EFFECTS.

Dr.

Cr.

		£ s d		INVESTMENTS:		£ s d		(m) State amount and description of stock.
(c) Where a single contribution provides more than one benefit, the lines may be bracketed together.	Amount of Sickness Fund (c)	..	..	1. In the Savings Bank, interest at	per cent.	..	..
	Amount of Death Fund ..	..	..	2. In the Public Funds (m)	..	..	..
	Amount of Annuity Fund ..	..	..	3. With the Commissioners for the reduction of the National Debt, interest at	per cent.	..	..
	Amount of Endowment Fund ..	..	..	4. Upon Government Securities in Great Britain or Ireland, interest at	per cent.	..	..
	Amount of Old Age Fund (where separate) ..	..	..	5. Upon Real Securities in Great Britain or Ireland, interest at an average of	per cent.	..	..
	Amount of Widows and Orphans' Fund (where separate) ..	..	..	6. In the Purchase of Land	..	..	..
	Amount of Lying-in Fund (where separate) ..	..	..	7. In the Erection of Offices and Buildings	..	..	..
	Amount of Accident Fund (where separate) ..	..	..	8. In Loans on Members' Assurances, under s. 18 (1) of Act, interest at	per cent.	..	..
	Amount of Travelling Benefit Fund (where separate) ..	..	..	9. In Loans out of Separate Loan Fund under s. 18 (2) of Act, interest at	per cent.	..	..
	Amount of Distress Relief Fund (where separate) ..	..	..	10. On other Securities (n)	..	..	..	(n) State them separately.
[If there are other benefit funds, state each separately.]	Amount of Surplus Fund accumulated for Members' use under s. 19 of Act ..	..	..	Cash in the Post Office Savings Bank	..	..	..	(o) State in whose hands.
	Amount of separate Loan Fund under s. 18 (2) of Act ..	..	..	Cash in hand (o)	..	..	..	(p) Specify them.
	Amount of other benefit funds, state each separately.]	..	..	Other Assets (if any) (p)	..	..	..
	Total Benefit Funds (as above)	..	..			
	Amount of Management Fund (as above)	..	..			
	Debits (if any) (f) legally incurred by Trustees on behalf of the Society	..	..			
	Cash due to Treasurer (if any)	..	..			
	Other Liabilities (if any) (g)	..	..			
	Total ..	..	..	Total ..	..	..	..	£
			£					

(n) State them separately.
(o) State in whose hands.
(p) Specify them.

* State Postal Address.

Signature of Treasurer or one of the Trustees _____ Signature of Secretary _____ residing at* _____

The undersigned, having had access to all the Books and Accounts of the Society, and having examined the foregoing General Statement, and verified the same with the Accounts and Vouchers relating thereto, now sign the same as found to be correct, duly vouched, and in accordance with law.

* Public Auditor : or _____ and _____ Auditors. Date _____ 1895.

* This term means only a Public Auditor appointed under the Friendly Societies Act.

If in any respect these accounts are incorrect, unvouched, or not in accordance with law, the Auditors are not to sign as above, but are to make a special report to the Society, of which a copy is to be sent to the Registrar with this Statement.

TRUSTEE SAVINGS BANKS.

THE TRUSTEE SAVINGS BANKS ACT, 1863.

26 and 27 Vict. c. 87.

No Savings Bank, subject to proviso hereinafter contained with respect to Branch Offices, &c., shall have benefit of this Act unless in Rules, &c., it shall be expressly provided as herein specified.

6.—No savings bank, subject to the proviso hereinafter contained with respect to the branch offices or local receivers of any savings bank, shall have the benefit of this Act unless in the rules and regulations for the management thereof it shall be expressly provided—

(1) That no person or persons being treasurer, trustee, or manager of such savings bank, or having any control in the management thereof, shall derive any benefit from any deposit made in such savings bank, save only and except such salaries and allowances or other necessary expenses as shall according to such rules and regulations be provided for the charges of managing such savings bank, and for remuneration to officers employed in the management thereof, exclusive of the treasurer or treasurers, trustee or trustees, manager or managers, or other persons having direction in the management of such savings bank, who shall not directly or indirectly have any salary, allowance, profit, or benefit whatsoever therefrom beyond their actual expenses for the purposes of such savings bank :

(2) That not less than two persons, being either trustees, managers, or paid officers appointed for that specific purpose, and where two only, except in the case of savings banks which are open for more than six hours in every week, one such person to be a trustee or manager, be present on all occasions of public business, and be parties to every transaction of deposit and repayment, so as to form at least a double check on every such transaction with depositors :

(3) That the depositor's Pass Book shall be compared with the Ledger on every transaction of repayment, and on its first production at the bank after each twentieth day of *November* :

(4) That every depositor in a savings bank established under this Act shall once at least in every year cause his deposit book to be produced at the office of the said savings bank for the purpose of being examined :

(5) That no money be received from or paid to depositors except at the office or branch offices where the business of the savings bank is carried on under the authority of the board of managers, and during the usual hours for public business.

(6) That a public accountant or one or more auditors be appointed by the trustees and managers, but not out of their own body, to examine the books of the banks, and to report in writing to the board or committee of management the result of such audit, not less than once in every half-year, also to examine an extracted list of the depositors' balances made up every year to the twentieth day of *November*, and to certify as to the correct amount of the liabilities and assets of the bank :

(7) That a book containing such extracted list of every depositors' balance, omitting the name, but giving the distinctive number and separate amount of each, and showing the aggregate number and amount of the whole, checked and certified by such public accountant or Auditors, be open at any time during the hours of public business for the inspection of every depositor as respects his own account, to examine his own Deposit Book therewith, and the general results of the same :

(8) That the trustees and managers or committee of management shall hold meetings once at least in every half-year, and shall keep minutes of their proceedings in a separate book provided for that purpose :

(9) Provided that where savings banks are established with agents or local receivers elsewhere than at the head office, the rules shall provide for the due receipt of, and accounting for, all moneys by such agents or local receivers on account of such savings banks respectively, and also for the presence of a second party in every transaction when money is paid or received, and also for the periodical examination of the depositors' books with the Ledger once at least in every year.

Weekly returns to be made by Savings Banks to the Commissioners.

7.—The trustees and managers of every savings bank shall transmit weekly returns to the Commissioners for the Reduction of the National Debt, in such form and giving such particulars as the said Commissioners may direct, showing the amounts of the week's transactions of such savings bank, and the amount of the cash balances remaining in the hands of the treasurer or any other person on account of such savings bank.

Trustees of Savings Banks shall Invest all Money in the Banks of England or Ireland and not in any other Security.

15.—The several sums of money belonging to any savings bank which the trustees of such savings bank respectively are authorised to invest under this Act or under any rules or regulations of any such savings bank shall, except as hereinafter is excepted, be paid into and vested in the Bank of *England* or the Bank of *Ireland*, as the case may require, in the names of the Commissioners for the Reduction of the National Debt according to the provisions of this Act, enabling such trustees to make investments in the names of the said Commissioners, and no such sum or sums shall be paid or laid out by the trustees of such savings bank in any other manner or upon any other security whatever, except as aforesaid, and except such sums of money as from time to time shall necessarily remain in the hands of the treasurer or treasurers of such savings bank to answer the exigencies thereof: Provided always, that nothing herein contained shall restrain or prevent any depositor, or any trustee or trustees acting on behalf of any depositor or depositors, or any friendly society, or any charitable or provident institution or society, or penny savings bank, from withdrawing from any such savings bank any sum or sums of money which shall have been deposited by such depositor, friendly society, charitable or provident institution or society, or penny savings bank, and investing the same in any other securities: Provided always, that the trustees of any savings bank already established, or which shall take the benefit of this Act in manner hereinbefore provided, shall be and they are hereby empowered to pay into the Bank of *England* or *Ireland* (as the case may be) any sum or sums of money, not being less than fifty pounds, to the account of the Commissioners for the Reduction of the National Debt, upon the declaration of the trustees of such savings bank, or any two or more of them, that such moneys belong exclusively to the savings bank for which such payment is intended to be made, whether such moneys shall have been deposited therein before the passing of this Act or thereafter shall be deposited therein, and the cashier or cashiers of the Banks of *England* and *Ireland* respectively are hereby required to receive all such moneys, and to place the same into the account raised in the names of the said Commissioners in the books of the Banks of *England* and *Ireland* respectively, denominated "The fund for the banks for savings": Provided, nevertheless, that previous to any payment being made into the Banks of *England* or *Ireland* as aforesaid, the person or persons applying for that purpose shall in all cases produce to the officer of the said Commissioners, at their office in *London* or *Dublin* (as the case may be), an order under the hands of two of the trustees of such savings banks on the account of which such payment is to be made.

Trustees not to receive from any one Depositor more than £30 in any one year.

39.—It shall not be lawful for the trustees of any savings bank to receive from any one present or future depositor, within any one year ending on the twentieth day of *November* (whether any sum or sums of money had been previously withdrawn or not) any sum or sums exceeding in the whole thirty pounds, exclusive of compound interest.

Provided that nothing in this Act, contained shall prevent or be construed to prevent the trustees of any savings bank from paying interest to any depositor whose deposit on the twenty-eighth day of *July* one thousand eight hundred and twenty-eight amounted to and has since continued to amount to or exceed the sum of two hundred pounds: nor to prevent any depositor, having closed his or her account in any savings bank, from making a deposit in the same or any other savings bank, not exceeding the limit allowed to be received in any one year from any new depositor.

Appointment of Auditors in Ireland.

51.—The trustees of each savings bank in *Ireland* shall, as soon as conveniently may be after the passing of this Act, and from time to time in case of a vacancy, appoint an Auditor or Auditors to audit the accounts of the said savings bank, as well as to examine and inspect the books of the several depositors, and the said trustees shall, immediately after such appointment, transmit the signature, name, and address of the said Auditor or Auditors to the Commissioners for the Reduction of the National Debt; and the trustees of every such savings bank in *Ireland* shall cause the annual and other statements required to be transmitted under this Act to be certified and verified by the Auditor or Auditors appointed by the said trustees, in addition to the attestation by trustees and managers, as also required by this Act, and shall also cause a certificate from the said Auditor or Auditors, as to the result of his or their examination of such of the depositors' books as may have been produced to him or them for examination, to be transmitted with the said annual statement to the said Commissioners: Provided always, that it shall be lawful for the trustees of any such savings bank in *Ireland* to agree with the trustees of any other such savings bank or banks in *Ireland* as to the appointment of a common Auditor or Auditors, and the Auditor or Auditors so appointed for all the said banks shall be deemed and taken, as soon as the signature, name, and address shall have been transmitted by each such bank to the said Commissioners, to be the Auditor or Auditors of each such bank.

Trustees of Savings Banks shall make up Annually Accounts of their Progress, &c., and transmit the same to the Commissioners for Reduction of the National Debt.

55.—For the more effectual ascertaining from time to time the actual and progressive state of the several savings banks enrolled under the provisions of this Act, the trustees and managers of every such savings bank shall annually cause a general statement of the funds of such savings bank invested in the Bank of *England* or the Bank of *Ireland* in the names of the Commissioners for the Reduction of the National Debt to be prepared up to the twentieth day of *November* in each year, showing the balance or principal sum due to all the depositors collectively in such savings bank, and a statement of the expenses incurred, and stating in whose hands such balance shall then be remaining; and every such annual statement shall be attested by two managers or two trustees, or by one manager and one trustee of such savings bank, and every such annual statement shall be countersigned by the secretary or actuary of such savings bank, and all such annual statements shall be transmitted to the office of the said Commissioners for the Reduction of the National Debt in *London* or *Dublin* (as the case may be) within nine weeks after the twentieth day of *November* in each year.

If Trustees neglect to transmit such Accounts or to obey any Orders given pursuant to this Act, Commissioners may close their Accounts, &c.

56.—And in case the trustees of any such savings bank shall neglect or refuse to make out and transmit such accounts as aforesaid, or in case any such trustees shall at any time neglect or refuse to obey any orders or directions given by the said Commissioners or through their officer, pursuant to the directions of this Act, it shall be lawful for the said Commissioners to close the account of the trustees of such savings bank, and to discontinue the keeping of any further account with the trustees of such savings bank, and to direct that no further sum shall be received at the Bank of *England* or at the Bank of *Ireland* from the trustees of such savings bank to the account of the said Commissioners until such time as such Commissioners shall think fit: Provided always, that it may be lawful for the said Commissioners to re-open such account, and to allow the growing interest of such account during the time of such discontinuance, and to authorise the receipt of money at the Bank of *England* or *Ireland*, whenever such Commissioners shall think fit to do so, upon such trustees complying with the directions of such Commissioners or their officer.

A Duplicate of such Account shall be affixed in the office of the Savings Bank.

59.—The trustees and managers of every such savings bank shall cause a duplicate of every such annual statement, accompanied by a list of the trustees and managers of such institution for the time being, attested and countersigned as aforesaid, to be publicly affixed and exhibited in some conspicuous part of the office or place where the deposits of such savings bank are usually received, for the information of all parties making deposits therein; and every such duplicate shall from time to time remain so affixed and exhibited until the ensuing annual statement shall in like manner be affixed and exhibited as aforesaid; and every depositor shall be entitled to receive from the said savings bank a printed copy of such annual statement on payment of one penny.

Savings Banks shall compute Interest on 20th May and 20th November half-yearly or yearly.

62.—For the purpose of rendering the accounts of the several savings banks in *Great Britain* and *Ireland* uniform and correspondent with the accounts of the Commissioners for the Reduction of the National Debt, the interest payable to the depositors in such savings banks in *Great Britain* and *Ireland* shall, from and after the 20th day of *November* one thousand eight hundred and sixty-three, be computed half-yearly to the twentieth day of *May* and the twentieth day of *November*, or yearly to the twentieth day of *November* in each year, as the case may be, and to no other periods.

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CHARGE	£ s d
To Balance due on 20th Nov.	
— as per last return ..	
To Sums received of Depositors	
in year ended 20th Nov.	
.. .. .	
To Sums transferred from Post Office Savings Banks	
To Sums transferred from other Savings Banks	
To Sums received for Stock sold for Depositors— <i>less Commission</i>	
To Interest on Moneys invested with the Commissioners for the Reduction of the National Debt, viz.:—	
Receipt B, dated May 21 ..	
Receipt B, dated Nov. 21 ..	
To Interest from Commissioners on sums drawn within the said year ..	
To Interest on sums transferred to Stock bought ..	
To Dividends on Stock ..	
To Commission on Stock ..	
To Allowance on Annuities ..	
	£

DISCHARGE	£ s d
By Sums paid to Depositors in year ending November 20th 1890 ..	
By Sums transferred to Post Office Savings Banks ..	
By Sums transferred to other Savings Banks ..	
By Sums paid for Stock bought for Depositors—including <i>Commission</i>	
By Sums paid for Management, viz.:—	
Salaries .. £	
Rent and Taxes ..	
Printing & Stationery ..	
Coal, Gas, and Water ..	
Petty Cash and Sundries ..	
Sums discharged for Building and Enlargement of Branch Offices ..	
Balance Invested with Commissioners on 20th Nov. — £	
Ditto on account of <i>Separate Surplus Fund</i>	
Ditto in the hands of the Treasurer and Actuary ..	
*Which fact is hereby certified by us.	£

No. of Depositors	CLASS	Total Amount of each Class
	Balance invested with Commissioners, &c., 20th Nov.—whose respective balances on the 20th Nov. — (including Interest) did not exceed £1 ..	£ s d
	Ditto where above £1 and not exceeding £5 ..	
" "	" " " £5 " £10 ..	
" "	" " " £10 " £15 ..	
" "	" " " £15 " £20 ..	
" "	" " " £20 " £30 ..	
" "	" " " £30 " £40 ..	
" "	" " " £40 " £50 ..	
" "	" " " £50 " £75 ..	
" "	" " " £75 " £100 ..	
" "	" " " £100 " £125 ..	
" "	" " " £125 " £150 ..	
" "	" " " £150 " " exceeding £200 on Accounts opened before the 28th July 1828 ..	
" "	" " " " " exceeding £200 on Accounts opened after the 28th July 1828* ..	
	Total Number of Depositors ..	
	Penny Savings Banks ..	
	Charitable Institutions, including Clothing Societies ..	
	Friendly Societies ..	
	Total Number of Accounts ..	
	Total Surplus ..	
	Deduct portion of above Surplus with Commissioners on the <i>Separate Surplus Fund Account</i> , on the 20th Nov. — ..	
	Surplus remaining on the General Account ..	
	*It is illegal to allow interest on these Accounts so long as they remain at or above £200 (26th and 27th Vic. cap. 87, sec. 39).	£

THE SAVINGS BANKS ACT, 1891.

*55 and 56 Vict. c. 21.**Establishment of Inspection Committee.*

2.—(1) There shall be established an inspection committee of trustee savings banks.

Powers and Duties of Inspection Committee.

3.—(4) The trustees of every trustee savings bank shall, on the requisition of the committee, supply the committee with a copy of the Pass Book in use in the bank, of the annual general statement of the accounts of the bank, and of the rules of the bank, and of any amendments thereof.

(5) If in the opinion of the committee the rules of any such bank are insufficient for the purpose of maintaining an efficient audit, the bank shall with all convenient speed make such additional rules as may, in the opinion of the committee, be required for the purpose.

(6) If the bank do not, within the time specified by the committee from the date of being required to make any such rules comply with the requirement, the committee may make such rules, and shall submit the rules so made to the Registrar of Friendly Societies, to be certified by him; and, when so certified, they shall be binding on the trustees.

Form of Annual Statement by Trustees of Trustee Savings Banks.

8.—The annual statement required by section fifty-five of the Trustee Savings Banks Act 1863 to be made by the trustees and managers of every trustee savings bank, shall be in such form and contain or be accompanied by such particulars as the National Debt Commissioners direct. A similar statement shall be sent to the inspection committee each year at the same time.

Amendment of Law as to limit of Deposit and Interest on Deposit.

11.—Whereas it is not lawful for the trustees of a savings bank or for the Postmaster-General to receive from any depositor any sum which shall make the sum to which such depositor shall be entitled exceed the sum of one hundred and fifty pounds in the whole, exclusive of interest, but the sum standing in the name of any depositor may be increased by accumulations of interest to any sum not exceeding two hundred pounds in the whole, and difficulties have arisen in the due apportionment between principal and interest of sums standing to the credit of

depositors in excess of one hundred and fifty pounds; be it therefore enacted as follows:—

(1) A savings bank shall not receive any deposit which makes the sum standing in the name of any depositor in the bank exceed two hundred pounds.

(2) So much of any enactment as prohibits the receipt from any depositor of any sum of money which makes the sum to which he is entitled exceed the sum of one hundred and fifty pounds in the whole exclusive of interest is hereby repealed.

(3) Interest shall be allowed in full on the sum standing in the name of a depositor in a savings bank so long as it does not exceed two hundred pounds, but whenever the sum standing in the name of any depositor in any savings bank exceeds that amount, interest shall not be allowed on any sum in excess of two hundred pounds.

(4) Notwithstanding any restriction on the amount to be deposited in any one year, a depositor in the savings bank may, not more than once in any savings bank year, deposit money to replace money previously withdrawn in one entire sum during that year. For the purposes of this provision the expression "savings bank year" means, with reference to trustee savings banks, the year ending the twentieth day of November, and with reference to the Post Office savings banks, the year ending the thirty-first day of December.

CO-OPERATIVE ACCOUNTS, &c.

THE INDUSTRIAL AND PROVIDENT SOCIETIES ACT, 1893.

56 and 57 Vict. c. 39.

Audit.

13.—(1) Every registered society shall, once at least in every year, submit its accounts for audit, either to one of the public Auditors in the Act mentioned, or to two or more persons appointed as the rules of the society provide.

(2) The Auditor shall have access to all the books, deeds, documents, and accounts of the society, and shall examine the Balance Sheets, showing the receipts and expenditure, funds and effects of the society,

and verify the same with the books, deeds, documents, accounts, and vouchers relating thereto, and shall either sign the same as found by them to be correct, duly vouched, and in accordance with law, or specially report to the society in what respects they find them incorrect, unvouched, or not in accordance with law.

Annual Returns.

14.—(1) Every registered society shall, once in every year, not later than the thirty-first day of March, send to the Registrar an annual return of the receipts and expenditure, funds and effects, of the society as audited.

(2) The annual return—

- (a) Shall be signed by the Auditor or Auditors ; and
- (b) shall show separately the expenditure in respect of the several objects of the society ; and
- (c) shall be made out from the date of its registration or last annual return to that of its last published Balance Sheet, provided that the last-named date is not more than one month before or after the thirty-first day of December then last, or otherwise to the said day of December inclusive ; and
- (d) shall state whether the audit has been conducted by a public Auditor appointed as by this Act is provided, and by whom, and if by any persons other than a public Auditor, shall state the name, address, and calling or profession of every such person, and the manner in which, and the authority under which, he is appointed.

The society shall, together with the annual return, send a copy of the report of the Auditors, or if more than one such report has been made during the period included in the return, a copy of each of such reports.

Supply of Copies of Annual Returns.

15.—Every registered society shall supply gratuitously to every member or person interested in the funds of the society, on his application, a copy of the last annual return of the society for the time being.

Copy of last Balance Sheet.

16.—Every registered society shall keep a copy of the last Balance Sheet for the time being, together with the report of the Auditors, always hung up in a conspicuous place, at the registered office of the society.

Public Auditors.

72.—The Treasury may appoint public Auditors for the purposes of this Act, and may determine the rates of remuneration to be paid by registered societies for the services of such Auditors, but the employment of such Auditors shall not be compulsory.

PUBLIC AUDITORS.

Official rates of payment :

For auditing the Accounts of Friendly Societies and specially authorised Societies granting Friendly Society benefits, the scale of payments shall be :—

	£	s	d
For Societies consisting of not more than 100 members ..	1	1	0
For Societies with over 100 members but not exceeding 500 members, in respect of each 100 members or part thereof..	1	1	0
For Societies consisting of over 500 members, in respect of the first 500 members	5	5	0
With an additional 10s. 6d. in respect of each additional 100 members or part thereof, no fee, however, to exceed £52 10s., unless by special arrangement.			

For auditing the Accounts of all other Societies registered under the Friendly Societies Acts, viz., Cattle Insurance Societies, Benevolent Societies, Working Men's Clubs, specially authorised Societies (except such as grant Friendly Society benefits), the scale of payment shall be :—

	£	s	d
For Societies whose total gross receipts do not exceed £2,000 per annum	1	1	0
For Societies whose total gross receipts exceed £2,000, but do not exceed £10,000 per annum, in respect of each £2,000 or fraction thereof	1	1	0
Where the gross receipts exceed £10,000 per annum, the fee to be fixed by private arrangement.			

For auditing the accounts of Industrial and Provident Societies, the scale of payment shall be :—

	£	s	d
For Societies whose total sales do not exceed £2,000 per annum	1	1	0

For Societies whose total sales exceed £2,000, but do not exceed £10,000 per annum, in respect of each £2,000 or fraction thereof	£	s	d
	1	1	0
For Societies whose total sales exceed £10,000, but do not exceed £25,000 per annum, in respect of the first £10,000..	5	5	0
With an additional 10s. 6d. in respect of each additional £2,000, or fraction thereof.			
Where the sales exceed £25,000 per annum, the fee to be fixed by special arrangement.			

The word "sales" in the case of societies for the buying and selling of land, to include instalments in repayment of advances.

The scales of fees apply only in cases where the society is located within the district assigned to the Auditor employed. If a society employs an Auditor appointed for any other district, special terms may be arranged. The Auditor may accept audits on terms lower than those of the above scale.

PUBLIC VALUERS.

When the benefits to be valued do not exceed two classes of sick allowance and deferred annuities, together with sums payable on the death of members and of their wives, the scales of payment to public valuers are as follows:—

Societies of not more than 75 members ..	£3	3	0
„ over 75 and not exceeding 100 ..	4	4	0
„ 100 „ „ 150 ..	5	5	0
„ 150 „ „ 200 ..	6	6	0
„ 200 „ „ 300 ..	7	7	0
„ 300 „ „ 400 ..	8	8	0
„ 400 „ „ 500 ..	9	9	0
„ 500 „ „ 600 ..	10	10	0
„ 600 „ „ 750 ..	12	12	0
„ 750 „ „ 1,000 ..	15	15	0

With a further £5 5s. for every 500 members or portion thereof beyond the total number of members not exceeding 2,500. Beyond 2,500 members the fee to be the matter of special arrangement, as well as in all cases where the number of benefits exceed that above mentioned. Valuers may accept valuation on terms lower than those of the above scale. Valuers must take such steps as they think fit for obtaining payment of their fees.

Note.—Employment of a Public Valuer under the Friendly Societies Act is not compulsory on any society.

THE COLLECTING SOCIETIES AND INDUSTRIAL
ASSURANCE COMPANIES ACT, 1896.

59 and 60 Vict. c. 26.

1.—This Act shall apply to every such—

- (a) Friendly society or branch, whether registered or unregistered (in this Act referred to as a collecting society); and
- (b) Person or body of persons, whether corporate or unincorporate, granting assurances on any one life for a less sum than twenty pounds (in this Act referred to as an industrial assurance company),

as receives contributions or premiums by means of collectors at a greater distance than ten miles from the registered office or principal place of business of the society or company, and, in the case of an industrial assurance company, at less periodical intervals than two months:

Provided that nothing in this Act shall, except as expressly provided thereby, apply to any assurance with an industrial assurance company the premiums in respect of which are receivable at greater periodical intervals than two months.

Balance Sheets and Annual Returns.

6.—(1) A copy of every Balance Sheet of a collecting society shall, during the seven days next preceding the meeting at which the Balance Sheet is to be presented, be kept open by the society for inspection at every office at which the business of the society is carried on, and shall be delivered or sent by post to every member on demand.

(2) The annual returns required to be sent to the Registrar under the Friendly Societies Act 1896 shall, in the case of a collecting society, be certified by some person not an officer of the society (otherwise than an Auditor thereof) carrying on publicly the business of an accountant, and if not so certified shall be deemed not to have been made.

Penalties for Falsification.

15.—If any person wilfully makes, orders, or allows to be made any entry, erasure in, or omission from a Contribution or Collecting Book with intent to falsify that book, or to evade any of the provisions of this Act, he shall be liable to a fine not exceeding fifty pounds, recoverable at the suit of the Chief or any Assistant Registrar, or of any person aggrieved.

APPENDIX B.

REPORTS OF CASES, THE DECISIONS OF WHICH ARE OF PROFESSIONAL INTEREST.

The case of THE LEEDS ESTATE BUILDING AND INVESTMENT
SOCIETY, LIM. *v.* SHEPHERD.

(Decided before Mr. Justice STIRLING, in the Chancery Division, on
9th August 1887.)

*Held to be an Auditor's duty to see that Accounts he Certifies are actually Correct—
Liability for Neglect.*

In 1869 the plaintiff company was formed and registered under the Act of 1862 for the purpose of dealing in lands and lending money on mortgage. In 1882 it went into voluntary liquidation.

By article 63 it was provided that when the company paid a dividend of 5 per cent. the directors were to receive 10s. for every meeting attended by them, and the remuneration was to be increased by 2s. 6d. for every additional 1 per cent. of dividend.

By articles 79 and 80 the directors were authorised to declare a dividend upon such estimate of profits as they might think proper to recommend, but no dividend was to be payable except out of profits.

Articles 86 to 89 provided that the directors should cause true accounts to be kept, and should lay before the company once in every year a statement of the income and expenditure, and also a Balance Sheet in the form prescribed by Table A of the Companies Act 1862.

Articles 90 to 101 related to the auditing of the accounts and provided that the Auditors should state in their report whether, in their opinion, the Balance Sheet was a full and fair Balance Sheet, properly drawn up so as to exhibit a true and correct view of the state of the company's affairs.

The articles also provided for the appointment of a manager and secretary, whose remuneration was to be fixed by the directors.

Except in 1876 the company made no profits during the whole period during which it carried on business.

This action was brought by the company in liquidation against the directors, the manager, and the Auditor of the company to make them liable in respect of certain sums paid out of capital for dividends, and for fees and bonuses to the directors and manager respectively.

The Balance Sheets were false and misleading and contained fictitious items, and were framed with a view to the declaration of dividend. They were prepared by the manager and examined by the Auditor. In examining the Balance Sheets the Auditor was not furnished with a copy of the articles, and he did not comply with their provisions. The directors did not investigate the accounts, but trusted entirely to the manager and the Auditor; and they did not know that the company had been paying dividends out of capital, or that the Balance Sheets were inaccurate. The Balance Sheets were not shown to the shareholders as required by the articles.

JUDGMENT.

Stirling, J., held, following *In re The Oxford Benefit Building and Investment Society* (56 L.J. Rep. Ch. 98), that the directors were bound to make good the several sums paid out of capital, and that the manager and Auditor were liable for damages to the like amount. With reference to the case against the Auditor, his Lordship said that it was the duty of the Auditor not to confine himself merely to the task of ascertaining the arithmetical accuracy of the Balance Sheet, but to see that it was a true and accurate representation of the company's affairs. It was no excuse that the Auditor had not seen the articles when he knew of their existence. The Statute of Limitations had been pleaded on his behalf, and the plea had not been resisted, so that his liability would be limited to the dividends paid within six years of the commencement of the action.

(L.J. Notes, 1887, p. 130.)

The (appeal in the) case of LEE *v.* NEUCHATEL ASPHALTE COMPANY, LIM.

(Decided before COTTON, LINDLEY, and LOPES, L.JJ., in the Court of Appeal, on 9th February 1889.)

Held that a Company may by its Articles of Association provide for the distribution of Profits arrived at before making good the depreciation of Fixed Assets—Application for Injunction refused.

The Court of Appeal delivered judgment in this important company case, which was argued before them on the 4th, 5th, and 6th inst., on an appeal by the plaintiff in the action from the decision of Mr. Justice

Stirling. The action was brought by Mr. Charles John Lee, on behalf of himself and all of the ordinary shareholders of the Neuchâtel Asphalte Company, against that company and the directors, one of whom, Mr. J. Varley, had been appointed to represent the preference shareholders of the company. The object of the action was to restrain the payment of a dividend of 9s. per share, proposed to be paid out of what were alleged by the defendants to be the profits of the company for the year ending December 31 1885. The company was on July 9 1873 incorporated under the Companies Act of 1862, with a capital of £1,150,000, divided into 35,000 preferred shares, and 80,000 ordinary shares, of £10 each respectively. One of the objects of the company, as defined by the memorandum of association, was to acquire, as from July 1 1873, and on the terms expressed in an agreement dated July 17 1873, a concession granted by the Government of the Canton of Neuchâtel, in Switzerland, and held by the Neuchâtel Rock Paving Company, and the exclusive right thereunder of getting the bituminous rock and mineral products from the Val de Travers, and also all the mines, works, business, property, and assets of the last-mentioned company, and also all the concessions held by five other companies, and all the businesses, properties, and assets of these various companies. The company had also power to work and get bituminous rock, according to any concession granted to the companies, and the product of any mines acquired by the company, and to sell and dispose of the same, and to carry on the business of manufacturers of asphalte and bituminous rock pavement in every branch, and also to grant concessions and establish subsidiary companies. By the agreement of July 17 1873, the Neuchâtel Company agreed to pay for the original concession and all the sub-concessions granted to the five subsidiary companies, and all the mines, properties, and assets of the reconstituted original company and the five subsidiary companies in fully paid preferred and ordinary shares in the Neuchâtel Company. Thus the selling companies were to be paid not on a valuation in cash, but in shares, and the whole of the ordinary shares of the defendant company and 33,700 out of the 35,000 preferred shares were to be allotted to the selling companies in consideration of the transfer to the Neuchâtel Company of their entire assets, including the concession granted by the Canton of Neuchâtel. The agreement was duly carried into effect, and the concessions, properties, and assets which were the subject-matter thereof were duly transferred to the Neuchâtel Company, and the 80,000 ordinary shares and 33,700 preferred shares duly allotted and issued to the selling companies. With a nominal exception, no other shares in the Neuchâtel Company had ever been issued. The articles of association of the company provided that no distribution of profits—except

an interim dividend not exceeding 7 per cent. on the preferred and 4 per cent. on the ordinary shares—should be made without the consent of a general meeting, whose decision was to be final in case of any dispute as to the amount of net profits; and it was provided by article 100 that the directors might, before recommending any dividend, set aside and invest out of the net profits of the company such sum as they thought proper as a reserved fund to meet contingencies or equalise dividends, or repair or maintain the company's works, but should not be bound to reserve moneys for the renewal or replacing of any lease or of the company's interest in any property or concession. The concession referred to in the agreement and in the memorandum of association was for a period of 20 years commencing December 15 1867, and ending December 14 1887, and conferred on the *cessionnaire* the exclusive right of working the asphalte mines within a certain defined area situate in the communes of Couvet and Travers, in the Canton of Neuchatel. The consideration for that concession originally consisted of a *minimum* annual rent of 40,000f. and a royalty of 19.75f. per ton of asphalte turned out; but for the 11 years between December 16 1870 and December 16 1881, these terms were modified as follows—there was to be paid a *minimum* annual rent of 100,000f. and a royalty varying from 19.75f. to 5f. per ton. After December 16 1881 the parties were to return to the terms of the original concession. Soon after that concession had, with the consent of the Government of the Canton, been transferred to the Neuchatel Company, it appeared from the annual reports of that company that the terms of it began to be felt unduly burdensome to the company, and negotiations were entered into for the modification and extension of it, and ultimately these were effected by a convention agreed on in November 1877, and finally adopted on January 22 1878. The more material modifications thus introduced were these—(1) The duration of the concession was extended for 20 years, so that instead of expiring on December 14 1887, it would not expire until December 14 1907; (2) the area under which the mines could be worked was very considerably enlarged; (3) the consideration for the modified concession consisted of (a) a present payment in cash of 200,000f. (£8,000), (b) a royalty of 6f. per ton of asphalte taken out of the mine, subject to a proviso that (c) if the annual working at the price of 6f. per ton should not produce 150,000f., the *cessionnaires* should nevertheless pay that amount by way of *minimum* royalty or dead rent. The result of the modification of the royalty as applied to the actual working of the company between the beginning of 1878 and the end of December 1885 was that the Government of Neuchatel had received about £39,000 less than would have come to it had the terms of the concession remained as they stood in 1873. The company had worked the mines and carried

on business from its formation down to the present time. For the year ending December 31 1879 the accounts showed an excess of receipts over expenditure to the amount of £8,165 12s. 1d., and in respect of this year's working a dividend amounting to 2s. 6d. per share, and making £4,252 10s., was for the first time declared. All the subsequent accounts showed a like excess of receipts over expenditure to a considerable extent. Dividends were declared for the years 1881, 1882, and 1883 of 5s., 3s. 6d., and 5s. per share. In 1884 no dividend was declared, although the accounts showed a balance of £39,359 to the balance of the Profit and Loss Account on December 31 1884; and this large sum was dealt with as follows—£1,000 was written off in respect of the sum paid for the modification and extension of the concession in 1877, and the balance of £38,359 was written off the cost in shares of the original concession and other assets taken over by the company on its formation. It appeared from the report for 1884 that the directors had resolved that the sum paid for the renewal of the concession should be written off at the rate of £1,000 a year. The accounts for the year 1885 showed an excess of receipts over expenditure to the amount of £17,140 13s. 2d., out of which, after setting aside a sum of £1,000 in reduction of the sum paid in 1887 for the renewal of the concession, it was recommended by the directors and resolved by a majority of the shareholders that a dividend on the preferred shares at the rate of 9s. a share should be paid. Mr. Justice Stirling, before whom the action was tried, dismissed the action, and the plaintiff now appealed.

JUDGMENT.

The Court dismissed the appeal.

Lord Justice Cotton, in giving judgment, after stating the nature and objects of the respondent company, and referring to the fact that the assets of the respondent company consisted of the concession and the other subsidiary rights taken over from the previously existing companies, and that these assets had not been paid for in cash, said:—Three points had been raised on behalf of the appellant. First, it was said that a principal part of the capital of the company had been lost. If by that it was meant that any part of the assets had been lost, in my opinion that is not correct, for the evidence shows that the assets of the company at present are of larger amount; its nominal capital, or, as I should prefer to call it, its share capital, is improved in value now to what it was when the company was formed in 1873, additional time for the concession to run having been obtained and less royalty having to be paid. Secondly, it was said that the property of the company was not sufficient to make good its nominal or share capital, and that the deficiency should be made up before any dividend ought to be

paid. In my opinion, that argument is entirely wrong and involves a misapplication of the term "capital." "Capital" is used in many senses, but the share capital of a company means the amount of its nominal capital divided into so many shares. The Companies Acts do not require, and it would be impossible that the assets of a company should be stated in its memorandum of association, though its share capital must be. No alteration can be made in the share capital of a company except in the manner provided for by the Companies Acts, and the share capital must not be applied except for some of the purposes for which the company was formed. But, in my opinion, there is no obligation on the company to make up the assets of the company so as to meet its share capital where the share capital has been issued under a duly registered contract, enabling allotment for something different from cash. Of course, if the contract was fraudulent or illusory, it might well be that the shareholders would be bound to pay up, in cash, the difference; but there is no suggestion of anything of that kind here. The payment of the proposed dividend, therefore, is not a return of capital; it is not a return of money which the shareholders were bound to provide in order to make up the nominal amount of their shares. The third point raised was one of more difficulty: it was said that this concession being a wasting property, the payment of this dividend was dividing part of the capital of the company represented by this concession. It is a well-established principle of company law that the capital assets of a company must not be applied for any purpose not one of the objects of the company, and though there is nothing in the Company Acts which says that dividends are not to be paid except out of profits—for the article to that effect in Table A in the schedule to the Act of 1862 is merely a matter of internal regulation—yet it is well established that the paying of a dividend is not one of the objects of a company, and therefore that the capital assets of a company must not be applied in that way. If the directors were to sell what was a permanent property of the company and then to declare a dividend, that would come within the principle laid down in *Guinness v. Land Corporation of Ireland* (L.R. 22 Ch.D. 349)—that the capital of a company cannot be applied for purposes not authorised. But that is not the case here, and we must take a reasonable and sensible view of the circumstances of this case. If it could be shown that this dividend was declared "for the purposes of fraud, or for any other improper motive, and that . . . the company has thereby in effect taken away from its creditors a portion of the capital which was available for their debts," to use the words of Lord Justice Selwyn in *Stringer's* case (L.R. 4 Ch. App., at p. 488), then this Court would interfere to prevent such improper dealing. But when the Court sees that the

directors of the company have acted fairly and reasonably in ascertaining whether this is in reality a part of the capital assets or not, then the Court is very unwilling to interfere with the discretion exercised by directors who have the management and regulation of the affairs of the company. In my opinion, it was not necessary, as Mr. Rigby suggested, that the directors should set apart each year a sum to answer the supposed annual diminution of this property by reason of its wasting nature. The Lord Justice then referred in detail to the cases of *Davison v. Gillies* (L.R. 14 Ch.D. 347n) and *Dent v. London Tramways Company* (L.R. 16 Ch.D. 344), which, he said, were consistent both with each other and with the view which he took in the present case, and said that, having regard to the nature and constitution of this mercantile company, he was not satisfied that a proper provision had not been made for depreciation by the establishment of a Reserve Fund, and considered that it would be wrong for the Court to interfere to prevent the payment of the proposed dividend.

Lord Justice Lindley agreed. His Lordship said the actual point to be decided is an easy one, but the difficulty arises from the fact that the Court is urged to lay down general principles of law, which, if adopted, would paralyse the whole trade of the country. The respondent company was formed for the purpose of working certain asphalte mines of which it had got a lease. It was quite obvious that with respect to such a property every ton of stuff got out of that which was bought with capital represented a portion of capital. It was said that a division of the profit arising from the sale of such was a return of capital. If that was so, it is not, at all events, such a return of capital as is prohibited by the Company Acts. There is nothing in any of the Company Acts prohibiting anything of the kind. The only provisions in those Acts relating to capital were Sections 8, 12, 26, 28, and 34 in the Act of 1862; Sections 9-20 in the Act of 1867; and Sections 3-5 in the amending Act of 1877. There was nothing in any of those sections as to the mode of payment of profits or dividends. It has been very judiciously and properly left to the commercial world to settle how the accounts were to be kept. The Acts do not say what expenses are to be charged to Capital Account and what to Revenue Account. Such matters were left to the shareholders; they may or may not have a sinking fund or a deterioration fund, the articles of association may or may not contain regulations on these matters; if they do, the regulations must be observed; if they do not, the shareholders can do as they like so long as they do not misapply their capital. In this case one of the articles provides that the directors shall not be bound to reserve moneys for the renewal or replacing of any lease or of the company's

interest in any property or concession. Mr. Rigby says that that provision in the articles is contrary to law. Now, the Companies Act 1862 does not require the capital to be made up if lost, and it does not prohibit payment of dividends so long as the assets are of less value than the capital called up, nor does it make loss of capital a ground for winding-up. The argument seems to be founded on the notion that the company is somehow a debtor to its capital; that may be a convenient notion from an accountant's point of view, but has nothing to do with law. Though the Acts do not say so, there are general principles of law which prohibit the capital of a company being applied for purposes other than those mentioned in the memorandum of association, and, further, if any of the purposes mentioned in the memorandum of association are expressly or impliedly forbidden by the statutes, then the capital of the company cannot be applied for those purposes (see *Trevor v. Whitworth*, 12 App. Cas. 409). But if a company is formed to acquire or work property of a wasting nature, *e.g.*, a mine, quarry, or patent, the capital expended in acquiring the property may be regarded as sunk and gone, and if the company retains assets sufficient to pay its debts, any excess of money obtained by working the property over the cost of working it may be divided among the shareholders; and this is true, although some portion of the property itself is sold, and in one sense the capital is thereby diminished. If it is said that such a course involves payment of dividends out of capital, the answer is that the Acts nowhere prohibit such a payment as is here supposed. The proposition that it is *ultra vires* to pay dividends out of capital is very apt to mislead, and must not be understood in such a way as to prohibit honest tradings. It is not true, as an abstract proposition, that no dividends can be properly declared out of moneys arising from the sale of property bought by capital. But it is true that if the working expenses exceed the current gains, profits cannot be divided, and that if in such a case capital is divided and paid away as dividend, the capital is misapplied, and the directors implicated in the misapplication may be compelled to make good the amount misapplied. This was the case in *Rance's* case (L.R. 6 Ch. App. 104); in the *Oxford Benefit Building Society's* case (L.R. 35 Ch.D. 502); in *Leeds, &c., Investment Company v. Shepherd* (L.R. 36 Ch.D. 787); and in *Stringer's* case (L.R. 4 Ch. App. 475). In the present case the articles say that there need be no sinking fund; consequently, capital lost need not be replaced; nor, having regard to these articles, need any loss of capital by removal of bituminous earth appear in the Profit and Loss Account of the working of the company's property. Our decision, therefore, in this case is quite consistent with the two cases before the late Master of the Rolls of *Davison v. Gillies* and *Dent v. London Tramways Company*.

Lord Justice Lopes: Very important questions are raised in this case. It is said by the appellants that a company is not to be at liberty to pay a dividend unless they can show that their available property at the time of declaring the dividend is equivalent to their nominal or share capital. In my opinion, such a contention is untenable. The nominal or share capital is diminished in value, not by means of any improper dealing with it by the company, but by reason of causes over which the company has no control or by reason of its inherent nature. That diminution need not, in my opinion, be made good out of revenue. In such a case a dividend may be paid out of current annual profits—out of profits arising from the excess of ordinary receipts over expenses properly chargeable to the Revenue Account, provided there is nothing contrary to the articles of association prohibiting such an application, and provided it is done honestly. If the contrary views were adopted, it might be successfully contended that where, owing to extraneous circumstances, the capital is increased in value, that increase might be dealt with as revenue profits and go to increase the dividend. That is contrary to all practice and to principle. It is said that where the capital is of a wasting character a sum must be laid aside to meet the depreciation, and that until such sum is laid aside there is nothing in the nature of profit divisible among the shareholders. The Lord Justice referred to the article providing that the directors should not be bound to reserve moneys for the renewal or replacing of any lease or of the company's interest in any property or concession, and proceeded:—Unless this article is *ultra vires* no question arises. Is the article *ultra vires*? I know of no obligation imposed by law or statute to create a Reserve Fund out of revenue to recoup the wasting nature of capital. Subject to any provision to the contrary contained in the articles, I believe the disposition of the revenue is entirely in the hands and under the control of the company. Provided there is by the company no infraction of the capital and nothing in the articles to the contrary, the disposition of the revenue is a matter of internal arrangement. I am unable to see in this case that either capital or the produce of capital has been dealt with in a way which is not authorised.

(*Acct. L.R.*, 1889, p. 26.)

The case of BOLTON v. NATAL LAND AND COLONISATION COMPANY, LIM.

(Decided before Mr. Justice ROMER, in the Chancery Division, on 8th, 9th, and 10th December 1891.)

Held that a Company may declare a Dividend out of current Profits without being obliged to show that all its Capital is intact.

The fact that some portion of the capital of an incorporated company limited by shares has been lost, and not made good, affords no

ground for restraining the payment of a dividend out of profits subsequently earned. The business of an incorporated company, limited by shares in the ordinary way, consisted mainly in buying, holding, cultivating, letting, selling, and otherwise dealing with land in South Africa. In 1882 the company, under peculiar circumstances, debited their Profit and Loss Account for that year with the whole loss occasioned by writing off a certain debt of over £70,000 as a bad debt, and *per contra* credited the same Profit and Loss Account with a sum of nearly £70,000 in respect of an increase in value attributed (rightly or wrongly) to their lands (or a portion of them) in South Africa, above and beyond the cost price at which such lands previously stood in the books of the company, the result being to make the Profit and Loss practically balance each other upon the year's accounts. The company, having subsequently earned a working profit, declared a dividend thereout, in respect of the year 1885. Thereupon the plaintiff, in an action commenced in 1886 to restrain the payment of such dividend, contended that, at the time the value of the lands was written up in 1882, they were valued, and now stood in the company's books at an amount considerably exceeding their true value, and that, before a profit could be deemed to have been made which would be properly available for the payment of a dividend, the lands in question must be written down to their true value, and the difference debited to the Profit and Loss Account, in the same way as the supposed increase had been credited to the Profit and Loss Account for the year 1882.

JUDGMENT.

Held, that, assuming that a part of the capital had in fact been lost, and not subsequently made good, no sufficient ground was thereby afforded for restraining the payment of the dividend; that the fact of the company having written up the value of their land in 1882, and credited the increase to the profit of that year in the manner described, did not place them under any obligation to bring into account in every subsequent year the increase or decrease in the value of their lands; and that, having regard to the case of *Lee v. The Neuchatel Asphalte Company* (61 L.T. Rep. N.S. 11; 41 Ch.D. 1), it was not correct, in estimating the profits of a year, to take into account the increase or decrease in the value of the capital assets of the company.

(92 L.T. Rep. 109.)

The case of **LUBBOCK v. THE BRITISH BANK OF SOUTH AMERICA, LIM.**

(Decided before Mr. Justice CHITTY, in the Chancery Division, on 1st April 1892.)

Held that if a Company's Articles of Association so provide, a Profit made on the Sale of a part of the Undertaking is available for Dividend.

This was a motion by the plaintiff, on behalf of himself and all others—the shareholders of the defendant company—to restrain the company

from acting upon or carrying into effect a resolution passed by the directors of the company on March 24 last, and from placing a sum of £205,000 to the Profit and Loss Account of the company, and from dealing with or distributing the same as if it were income of the company. It was stated that the company was incorporated in 1863 for the purpose of carrying on a banking business, with a capital of £1,000,000 divided into 100,000 shares of £10 each. All the shares of the company had been issued with £5 each paid up, constituting a paid-up capital of £500,000. The company had carried on business all over the world, but chiefly in America. Up to July 1891, the name of the company was the English Bank of Rio de Janeiro, but in January 1891 an agreement was entered into between the company and a Brazilian bank—namely, the Banco de Credito Universal (of Rio de Janeiro)—for the sale by the company of its goodwill and property in Brazil to the Brazilian bank for a sum of £875,000, and the company also agreed on the payment of the £875,000 to discontinue the use of its name, and to adopt a name not indicating a bank doing business in Brazil, and the agreement contained provisions restricting the company from carrying on business in Brazil. At the end of June all the £875,000 was paid. In November the restriction against the company's carrying on business in Brazil was released by the Brazilian bank on payment by the company to the latter of £75,000. The £205,000 in question was the net balance of the £875,000, after deducting the £500,000 paid-up capital of the company, the £75,000 repayment, and divers sums for outgoings and compensation in reference to the sale to the Brazilian bank. On March 24 last a resolution was passed by the directors that the profit derived from the sale and repurchase of the bank's business in Brazil be treated as profit to be carried to the Profit and Loss Account of the bank, and dealt with accordingly. It was stated that the present proceedings were of a friendly character, both parties being desirous of obtaining the opinion of the Court.

Mr. Whitehorne, Q.C., and Mr. S. Dickinson, in support of the motion, submitted that to carry over the £205,000 to a Profit and Loss Account appeared to be *ultra vires* the company, as, according to the authorities, *Frames v. Bultfontein Mining Company* (L.R. 1, Ch. 1891, 140), *Lee v. Neuchâtel Asphalte Company* (L.R. 41 Ch.D. 1, *per* Lord Justice Lopes, p. 26), a sum like the present, produced by the sale of part of the undertaking of the company, and not by earnings, should be treated as an accretion of capital to be placed to the Capital Account, and it was also argued that, having regard to the statements issued to the shareholders by the directors with regard to this particular

fund, it was not competent for the directors to act on the resolution in question or carry the fund to the Profit and Loss Account.

Mr. Byrne, Q.C., and Mr. Methold appeared for the company.

JUDGMENT.

Mr. Justice Chitty held that the £205,000 was plainly profit on capital, and not part of the capital itself, for that sum was the surplus ascertained on the assets' side after the liabilities and capital were placed on one side of the account and the assets on the other. Under the articles of the company the directors were justified in carrying over the £205,000 to a Profit and Loss Account, and having appropriated to the Reserve Fund so much of the sum as they thought fit, they could distribute the remainder as dividends after an ordinary meeting called in pursuance of the articles had passed the requisite resolution.

(*Acct. L.R.*, 1892, p. 56.)

The case of THE EDINBURGH UNITED BREWERIES, LIM.,
AND OTHERS *v.* JAMES A. MOLLESON (NICHOLSON'S
TRUSTEE) AND ANOTHER.

(Decided in the Scottish Court of Appeal before the LORD PRESIDENT,
and Lords ADAM, M'LAREN, and KINNEAR, on 17th March 1893.)

Held that a Contract of Sale of a Business cannot be upset on the ground that the Accounts submitted for Inspection prior to Purchase turn out to be false, provided the Sale was made bonâ fide and without Warranty.

In this action the Edinburgh United Breweries, Lim., and William H. Dunn, 27 Bishopsgate Street, London, sued James A. Molleson, C.A., Edinburgh, as trustee of David Nicholson, Parson's Green, for the reduction of the sale of the Palace Brewery, on the ground that the books had been falsified in order to show a larger profit than that actually earned during the two years preceding the sale. Lord Kyllachy assolized the defenders, with expenses, on the ground that if there was a fraud the pursuer had opportunity of discovering it by examination of the books. The pursuers reclaimed, and to-day the Court, following Lord M'Laren, adhered to the judgment of the Lord Ordinary, with expenses.

JUDGMENT.

Lord M'Laren, who gave the judgment of the Court, said the case was peculiar in this respect, that while the action was laid on the ground of fraudulent representations, no personal fault was

attributable to Mr. Molleson, who was known to be a gentleman of high standing in his profession. The case against him was that he employed Andrew Smith Geddes to keep the books of the brewery while it was under his management as trustee; that Geddes, for his own purposes, falsified the books and the Balance Sheets; that Mr. Dunn was induced to become the purchaser in reliance on the apparent profits exhibited on the face of the books and Balance Sheets, and was in that sense deceived by representations for which it was said Mr. Molleson was civilly responsible. So far as his Lordship understood, Geddes had no motive to falsify the books beyond the wish to please his employer and keep his situation by giving an aspect of fictitious prosperity to the business. By the agreement of November between Mr. Molleson and Mr. Dunn the sum of £3,700 was to be paid down, and the balance of the price was to be paid on 31st December, when the conveyance was granted. By the tenth clause of that agreement it was provided that the arrangement proceeded upon the basis that the net profits from the brewery and wine businesses during each of the two years 1887 and 1888 amounted to £3,750, or thereabout, upon an average; and in the event of its being ascertained that that was not the fact, this arrangement should be at an end, and the second party (Mr. Molleson) should be bound to repay the sum of £3,700. The first party (Mr. Dunn), with the view of verifying the amount of the profits for the two years, should be entitled to have the books, accounts, and vouchers connected with the businesses examined by an accountant named by him. The question was whether Mr. Molleson, as vendor, was affected by the fact that false entries were made in the books by the clerk Geddes for the purpose of bringing out an apparent profit in excess of the real profit. The excess was stated at £1,250, but the exact sum was immaterial to the present inquiry. It was a condition of the bargain that the books had to be delivered to the purchaser for examination, and his Lordship thought that condition was not fulfilled by delivering dishonest books. It was just the same as giving no books at all; and his Lordship had come to the conclusion that Mr. Dunn was not barred by the 10th article from challenging the sale on the ground of fraudulent representations as to the profits of the business, because he only agreed to take the risk of profits on the condition that books containing a true record of the brewery transactions should be submitted to him for examination. But, while his Lordship held it to be established that a fraud was committed inducing Mr. Dunn to enter into the contract, it did not follow that the pursuers, severally or collectively, were in a position to enforce the claim of restitution. The really important question was whether Mr. Dunn had a right to reduce his contract of sale—such a right as he could communicate to the

United Breweries, to whom he had sold the brewery for £28,500, the price he paid to Mr. Molleson being £20,500. Mr. Dunn resold the brewery at a profit, and he was not proposing to relinquish the profit of £8,000 which came to him indirectly through the false impression which the books produced on the minds of the purchasers from him. On the discovery of the fraud which had been practised upon him, Mr. Dunn was under no obligation to cancel the sale to the United Breweries. He had sold to them in good faith and without warranty. If Mr. Dunn proposed to repay the £8,000 on the ground that he could not conscientiously retain it, and to assign his claim of restitution against Mr. Molleson in order that the United Breweries might obtain redress, he would have found in him (Lord M'Laren) a convinced partisan of the duty of restitution. It would be no answer to him to say that he had the means of recouping himself by holding the United Breweries to their bargain. A purchaser in such a case was entitled to say—"I refuse to take a benefit which has been obtained by fraud: and I will neither hold my purchaser to his engagements nor will I submit to be bound by the deception which has been practised on myself." His Lordship was not imputing any blame to Mr. Dunn, or to the parties whom he represented, because they had not begun by making restitution. He did not know that they had been asked to do so. He only wished to put their case in a clear light. He understood Mr. Dunn's position to be this—that he meant to keep the £8,000, which he was enabled to make by the exhibition of forged books and fraudulent Balance Sheets, and at the same time to try and cut down his title to the subject of sale on the ground that the title was vitiated by that very fraud. It was clear that, if Dunn were suing by himself alone, it would be a conclusive answer to his claim that he had sold the subjects at a price calculated on the erroneous value attributed to the subjects, that he had not repaid the price to his sub-vendor, and that he had, therefore, made a profit out of the fraud. The circumstance that he had bought back the property, and was thus enabled to offer restitution, would not, in his Lordship's judgment, improve his position. Plainly Dunn could communicate no higher right to the United Breweries than he himself possessed. The United Breweries had no direct claim of any kind either against Molleson or against Dunn. Whatever right of action they might acquire through Dunn, by being joined with him as pursuers, must be measured by his right, and it followed that the action, considered as an action at the instance of the United Breweries, must also fail.

Their Lordships concurred.

(*Acct.* 1893, p. 301.)

The case of *VERNER v. THE GENERAL AND COMMERCIAL INVESTMENT TRUST, LIM.*

(Decided before Lords Justices LINDLEY, KAY, and SMITH, in the Court of Appeal, on 7th April 1894.)

Held that an Injunction to restrain a Company from paying a proposed Dividend out of current Profits on the ground that the Capital of the Company is not intact, must be refused if the Company is solvent, and acting within its Articles.

This was an appeal from a decision of Mr. Justice Stirling. It raised a very important question in company law—viz., whether, where there has been a loss in the capital of a company through depreciation in the value of its assets, the company is entitled to pay dividends out of profits earned by means of its investments without first reducing its capital so as to meet such depreciation. The action was brought by William Henry Verner, on behalf of himself and all other stockholders of the defendant company other than the directors, against the company and the directors. It came before the Court upon a motion by the plaintiff asking that the defendants might be restrained from declaring and from distributing among the members of the company any dividend in respect of the financial year of the company terminating on February 28 1894. The company was incorporated on January 26 1888, under a memorandum and articles of association, with a capital of £600,000 in 60,000 shares of £10 each, all of which had been issued and fully paid up in cash and converted into stock of two classes—preferred and deferred. In addition to its original share capital the company had borrowed £300,000 on the security of debenture stock, bearing interest at 4 per cent., and secured by a floating charge upon all the assets of the company. There had thus come to the hands of the company £900,000, which had been invested in various securities authorised by the memorandum of association. The present market value of such investments was only £654,776, showing a depreciation of £240,000. According to the evidence of the plaintiff it appeared that “of such depreciation £75,000 or thereabouts represented the amount which there was no prospect of recovering within any reasonable period of time.” During the past year the receipts of the company in respect of income derived from their investments had exceeded the expenditure by upwards of £23,000. The question for the Court upon the motion was whether, there being a loss of capital to the amount of £75,000 and an excess of profits over expenditure of £23,000, a dividend could lawfully be declared and paid. The company was formed for the purpose of raising money and investing the same in various investments mentioned in the memorandum of association, and one of the objects of the company was “to receive the dividends, income, profits, bonuses, and

advantages of every description from time to time payable or receivable in respect of the company's investments, and to apply the same respectively according to the provisions of the articles of association in force for the time being." The articles provided:—(84) "Subject to the rights of members holding share capital issued upon special conditions the receipts of the company from the dividends, income, profits, bonuses, and advantages payable or receivable in respect of the company's investments shall be applicable as follows:—First, to the payment of a dividend for the particular year at the rate of 5 per cent. per annum on the preferred stock; second, to the payment of such a dividend on the deferred stock as the same shall suffice to pay, and the trustees may, with the sanction of the company in general meeting, declare a dividend to be paid to the members accordingly." (85) "The trustees may, before recommending any dividend, set aside out of the profits of the company such sum as they think proper as a Reserve Fund to meet contingencies, or for equalising dividends, or for any other purposes of the company; and may from time to time apply the whole or any part of such fund for any purposes of the company." Mr. Justice Stirling, having regard to the nature of the constitution of this company, held that there was no legal obligation on the part of the company to make good the loss arising from the diminution in the value of the investments before declaring a dividend, and he dismissed the action. The plaintiff appealed.

Mr. Graham Hastings, Q.C., and Mr. Kirby were for the appellant; Mr. Buckley, Q.C., and Mr. Eve were for the respondents.

The Court dismissed the appeal.

JUDGMENT.

Lord Justice Lindley delivered the judgment of himself and Lord Justice A. L. Smith as follows:—The broad question raised by this appeal is whether a limited company which has lost part of its capital can lawfully declare or pay a dividend without first making good the capital which has been lost. I have no doubt it can—that is to say, there is no law which prevents it in all cases and under all circumstances. Such a proceeding may sometimes be very imprudent, but a proceeding may be perfectly legal and may yet be opposed to sound commercial principles. We, however, have only to consider the legality or illegality of what is complained of. As was pointed out in *Lee v. Neuchâtel Asphalte Company* (41 Ch.D. 1), there are certain provisions in the Companies Acts relating to the capital of limited companies; but no provisions whatever as to the payment of dividends or the division of profits. Each company is left to make out its own regulations as to such payment or division. The statutes do not even

expressly and in plain language prohibit a payment of dividend out of capital. But the provisions as to capital, when carefully studied, are wholly inconsistent with the return of capital to the shareholders, whether in the shape of dividends or otherwise, except, of course, on a winding-up, and there can, in my opinion, be no doubt that even if a memorandum of association contained a provision for paying dividends out of a capital such provision would be invalid. The fact is that the main condition of limited liability is that the capital of a limited company shall be applied for the purposes for which the company is formed, and that to return the capital to the shareholders either in the shape of dividend or otherwise is not such a purpose as the Legislature contemplated. But there is a vast difference between paying dividends out of capital and paying dividends out of other money belonging to the company, and which is not part of the capital mentioned in the company's memorandum of association. The capital of a company is intended for use in some trade or business, and is necessarily exposed to risk of loss. As explained in *Lee v. Neuchâtel Asphalte Company*, the capital even of a limited company is not a debt owing by it to its shareholders, and if the capital is lost the company is under no legal obligation either to make it good or, on that ground only, to wind up its affairs. If, therefore, the company has any assets which are not its capital within the meaning of the Companies Acts, there is no law which prohibits the division of such assets amongst the shareholders. Further, it was decided in that case, and, in my opinion, rightly decided, that a limited company formed to purchase and work a wasting property, such as a leasehold quarry, might lawfully declare and pay dividends out of the money produced by working such wasting property without setting aside part of that money to keep the capital up to its original amount. There is no law which prevents a company from sinking its capital in the purchase or production of a money-making property or undertaking, and in dividing the money annually yielded by it without preserving the capital sunk so as to be able to reproduce it intact either before or after the winding-up of the company. A company may be formed upon the principle that no dividends shall be declared unless the capital is kept undiminished, or a company may contract with its creditors to keep its capital or assets up to a given value. But in the absence of some special article or contract there is no law to this effect, and, in my opinion, for very good reasons. It would, in my judgment, be most inexpedient to lay down a hard and fast rule which would prevent a flourishing company either not in debt or well able to pay its debts from paying dividends so long as its capital sunk in creating the business was not represented by assets which would, if sold, reproduce in money the capital sunk. Even a sinking fund to

replace lost capital by degrees is not required by law. It is obvious that dividends cannot be paid out of capital which is lost: they can only be paid out of money which exists and can be divided. Moreover, when it is said, and said truly, that dividends are not to be paid out of capital, the word "capital" means the money subscribed pursuant to the memorandum of association, or what is represented by that money. Accretions to that capital may be realised and turned into money which may be divided amongst the shareholders, as was decided in *Lubbock v. British Bank of South America* (1892, 2 Ch. 199). But, although there is nothing in the statutes requiring even a limited company to keep up its capital, and there is no prohibition against payment of dividends out of any other of the company's assets, it does not follow that dividends may be lawfully paid out of other assets regardless of the debts and liabilities of the company. A dividend presupposes a profit in some shape, and to divide as dividend the receipts say, for a year, without deducting the expenses incurred in that year in producing the receipts, would be as unjustifiable in point of law as it would be reckless and blameworthy in the eyes of business men. The same observation applies to payment of dividends out of borrowed money. Further, if the income of any year arises from a consumption in that year of what may be called circulating capital, the division of such income as dividend without replacing the capital consumed in producing it will be a payment of a dividend out of capital within the meaning of the prohibition which I have endeavoured to explain. It has been already said that dividends pre-suppose profits of some sort, and this is unquestionably true. But the word "profits" is by no means free from ambiguity. The law is much more accurately expressed by saying that dividends cannot be paid out of capital than by saying that they can only be paid out of profits. The last expression leads to the inferences that the capital must always be kept up and be represented by assets which, if sold, would produce it; and this is more than is required by law. Perhaps the shortest way of expressing the distinction which I am endeavouring to explain is to say that fixed capital may be sunk and lost, and yet that the excess of current receipts over current payments may be divided, but that floating or circulating capital must be kept up, as otherwise it will enter into and form part of such excess, in which case to divide such excess without deducting the capital which forms part of it will be contrary to law. The Companies Acts do not require even limited companies to keep accounts, still less to keep them in any particular form. The only enactment on the subject is Section 26 of the Companies Act 1862, and Form D in the third schedule, and these relate solely to the nominal capital and calls. But although this is so, yet, as a matter of business,

accounts of some sort must be kept, and in order to show what has been subscribed by the shareholders and what has become of the money so subscribed, and to show the results of the company's trading or business, it is practically necessary to keep a Capital Account, and what is called a Profit and Loss Account, and as a matter of business these accounts ought to be kept as business men usually keep them. Accordingly, we find provisions for keeping such accounts in Table A in the Appendix to the Companies Act 1862 (see articles 78-82), and in the articles of association of most, if not all, companies. But there is no law which compels limited companies in all cases to recoup losses shown by the Capital Account out of the receipts shown in the Profit and Loss Account, although care must be taken not to treat capital as if it were profit. This is in accordance with *Bolton v. Natal Land Company* (1892, 2 Ch. 124), which is the latest reported case on the subject. Further, it is obvious that capital lost must not appear in the accounts as still existing intact; the accounts must show the truth and not be misleading or fraudulent. The Acts of 1867 and 1877 are in no way inconsistent with these observations. They provide for the reduction of the nominal capital mentioned in the memorandum of association. They do not render it obligatory on a company which has lost some of its capital to reduce the nominal amount mentioned in its memorandum. There are advantages in doing so, and the Acts were passed to enable limited companies to obtain these advantages, but there is nothing in these Acts, any more than in the Act of 1862, which prevents a company which has lost part of its capital from continuing to carry on business and declaring and paying dividends. A law forbidding this may well have been considered by the Legislature far too rigid, and in their desire to check dishonest and reckless trading, Courts must be careful not to put tighter fetters on companies than the Legislature has authorised. It follows from what has been said above that the proposed payment of dividend in this particular case cannot be restrained. Mr. Justice Stirling has, in his judgment, examined the memorandum and articles of association so fully that I do not think it necessary to examine them again. It is plain there is nothing in them which requires lost capital to be made good before dividends can be declared. On the contrary, they are so framed as to authorise the sinking of capital in the purchase of speculative stocks, funds, and securities, and the payment of dividends out of whatever interest, dividends, or other income such stocks, funds, and securities yield, although some of them are hopelessly bad, and the capital sunk in obtaining them is lost beyond recovery. There is no suggestion of any improper juggling with the accounts, and there is no payment of dividend out of capital. There is no insolvency, and we have not to deal with a petition to wind up.

Some capital is lost, but that is all that can be truly said, and that is not enough to justify such an injunction as is sought. The appeal must be dismissed.

Lord Justice Kay gave judgment to the same effect.

(*Times*, 8 April 1894.)

The case of WILMER v. M'NAMARA & Co., LIM.

(Decided before Mr. Justice STIRLING, in the Chancery Division,
on 26th April 1895.)

Held that a Company cannot be restrained from declaring a Dividend out of current Profits, because no provision has been made for Depreciation of Fixed Assets.

This was a motion on behalf of the ordinary shareholders of the defendant company asking for an injunction to restrain the directors from acting upon a resolution passed at a general meeting of the company, that a sum of £5,816 12s. 6d. should be applied in payment of a dividend to the preference shareholders, and also from declaring or paying any dividend for the year ending the 30th June 1894. The real object of the action, which was a friendly one, was to ascertain whether or not the dividend in question could be lawfully paid. The defendant company was formed in 1887 to acquire and develop a carrier's business previously known as Arthur M'Namara & Co., and to carry on the business of general carriers of mails, parcels, goods, &c. The capital of the company was £120,000, divided into 12,000 shares of £10 each, 7,000 of which were preference shares, carrying a fixed preferential cumulative dividend at the rate of 8 per cent. per annum, and the remaining £5,000 were ordinary shares, the holders thereof dividing all surplus profits after payment of the said preferential dividend. By an agreement dated the 8th of July 1887, the company agreed to purchase the business in question, including the goodwill, leasehold premises, horses, vans, plant, &c., thereunto belonging, for the sum of £54,000 in cash and 5,000 ordinary shares, which were to be deemed fully paid-up. The 7,000 preference shares were offered to and taken up by the public, being fully paid-up in cash, the vendors receiving their purchase-money (£54,000) thereout. At the end of the first year of the company's existence (the 30th of June 1888) an allowance of £3,810 was made in the accounts for depreciation in the value of the leases, goodwill, and plant, and in each of the following years up to and including 1891 an allowance of £2,000 was made for the like purpose. In 1892, however, the allowance in respect of this account was only

£250; but in all of these years there were substantial charges against income for van-maintenance, horses, and repairs to buildings. A valuation made for the year ending the 30th of June 1893 showed assets about £62,800, goodwill £20,000, and liabilities £12,400, leaving a balance of £70,400. No dividend was either declared or paid in this year. For the year ending the 30th June 1894 a like valuation showed a balance of £76,250, the Profit and Loss Account on that year's working showing a balance of £5,816 12s. 6d. to the good. By a resolution passed at a meeting of the company held on the 11th of September 1894, it was resolved that the said sum of £5,816 12s. 6d. should be applied in payment of a dividend to the preference shareholders. This was a motion by the ordinary shareholders to restrain the directors of the company from acting upon the said resolution, on the ground that until the loss of capital had been made up no dividends ought to be paid. The company was solvent, and the subject in dispute affected the shareholders alone. A scheme had been prepared for the reduction of the capital of the company, but it had fallen through. The real question was whether or not the proposed dividend could be lawfully paid.

JUDGMENT.

Stirling, J., after stating the facts as above set out, delivered a reserved judgment, as follows:—The nominal share capital of the defendant company amounts to £120,000, and the assets at the date of the last valuation fell short of that sum by over £43,000. Of the capital, however, only £70,000 was received in cash, the remaining £50,000 being paid over to the vendors in the form of 5,000 ordinary shares of £10 each fully paid, in part payment of the purchase-money due to them. Under these circumstances the decision in the case of *Lee v. Neuchâtel Asphalte Company* (37 W.R. 247, 41 Ch.D. 1) applies to this extent—i.e., that dividends may be paid although the assets are not sufficient to make up the nominal amount of the share capital. Beyond this, however, the case does not assist in point of decision, for in that case the assets of the company were at the period in question of greater value than they were at the date of the formation of the company. In a later case, however, *Verner v. General Investment Trust* (1894, 2 Ch. 239), the Court of Appeal laid down that in determining whether a dividend might or might not be paid by a company, regard was to be had to the constitution of the company and its articles. Lindley, L.J., at page 265, says: "A company may be formed upon the principle that no dividend shall be declared unless the capital is kept undiminished, or a company may contract with its creditors to keep its capital or assets up to a given value, but in the absence of some special article or contract, there is no law to this effect." Here there is no such contract with

creditors, and it is, therefore, only necessary to consider the articles of association, which closely resemble those in Table A to the Companies Act 1862. Article 117 provides that "no dividend shall be payable except out of the profits arising out of the business of the company." What are these profits? [Upon this point his Lordship referred at some length to the judgment of Lindley, L.J., in *Verner v. General Investment Trust* (*supra*), and continued.] Apart from the use of the word "profits" in article 117, there is nothing in the articles to show that the capital of the company (or, rather, assets of the value of those acquired by the company at its formation) must be kept up. Further, the articles appear to contemplate "profits" as the excess of receipts over all expenditure properly attributable to the year. It is necessary, however, to consider whether the depreciation in goodwill and leaseholds is to be treated as loss of "fixed" capital or of "floating" or "circulating" capital, and on this point I am of opinion that it is to be treated as loss of "fixed" capital. It very closely resembles the loss which a railway company may be said to suffer if it be found that their line, which was made, say, ten years ago, at a certain cost, could now be made at a much smaller cost. Having regard to the remarks of Lindley, L.J., in *Lee v. Neuchâtel Asphalte Company* (*supra*), I think that the Balance Sheet cannot be impeached simply because it does not charge anything against revenue in respect of goodwill. I feel much more doubt whether £200 is a sufficient sum to allow in respect of depreciation of leaseholds, but I do not think under the circumstances that a case has been made out for an injunction, and the motion must be refused.

(39 S.J. 450.)

The case of THE LONDON AND GENERAL BANK, LIM.

(Decided before Lords Justices LINDLEY, LOPES, and KAY, in the Court of Appeal, on 30th April 1895.)

Held that the Auditor of a Company, registered under the Companies Act, 1879, is an "Officer" of that Company within the meaning of the Companies (Winding-up) Act, 1890.

There are four appeals in this case against a judgment of Mr. Justice Vaughan Williams, by which he held that certain directors and Auditors of the above company (now in liquidation) were liable to make good to the assets of the company some large sums, which had been paid as half-yearly dividends upon the capital of the company, on the ground

that those sums had not been paid out of the profits of the company, but out of the capital, and that the payments constituted a misapplication of the funds of the company, for which the directors and Auditors were liable under what is known as the "misfeasance" section—Section 10—of the Companies (Winding-up) Act 1890. The company was connected with what is generally known as "the Balfour Group" of companies. The appeals are brought respectively by three of the directors—Messrs. S. Walker, A. T. Layton, and S. R. Pattison—and one of the Auditors, Mr. W. Theobald. Section 10 of the Companies Act 1890 is as follows:—"Where in the course of the winding-up of a company under the Companies Acts it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager, liquidator, or other officer of the company, has misapplied or retained, or become liable or accountable for, any moneys or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may, on the application of the Official Receiver, or of the liquidator of the company, or of any creditor or contributory of the company, examine into the conduct of such promoter, director, manager, liquidator, or other officer of the company, and compel him to repay any moneys or restore any property so misapplied or retained, or for which he has become liable or accountable, together with interest after such rate as the Court thinks just, or to contribute such sums of money to the assets of the company by way of compensation in respect of such misapplication, retainer, misfeasance, or breach of trust, as the Court thinks just." The company was formed subsequently to the passing of the Companies Act 1879, Section 7 of which provides, Sub-section 1—"Once at the least in every year the accounts of every banking company registered after the passing of this Act as a limited company shall be examined by an Auditor or Auditors, who shall be elected annually by the company in general meeting." Sub-section 2 disqualifies directors and officers from being Auditors. Sub-section 5 gives Auditors right of access to books and documents. Sub-section 6 provides that the Auditors shall make proper reports to the shareholders, and especially whether the Balance Sheets referred to in these reports are full and fair.

Sir E. Clarke, Q.C., and Mr. Germaine are for Mr. Walker; Mr. Herbert Reed, Q.C., and Mr. F. Low are for Mr. Layton; Mr. Cohen, Q.C., Mr. Cozens-Hardy, Q.C., and Mr. F. Whinney are for Mr. Theobald; Mr. Coleridge is for Mr. Pattison; Mr. Finlay, Q.C., Mr. E. S. Ford, and Mr. Muir Mackenzie are for the Official Receiver and liquidator.

The appeal was partly heard by their Lordships on Thursday and Friday last week. They reserved judgment until this morning on the

question whether an Auditor was an officer within the summary jurisdiction of the Court under Section 10 of the Winding-up Act, and, upon a suggestion that some matter had been improperly admitted as evidence by Mr. Justice Vaughan Williams, intimated that they might refer it to an official referee to inquire into and report whether there had been payments of dividends out of capital.

JUDGMENT.

Lindley, L.J. : The question which has been submitted to us in this case is, whether an Auditor of this bank can be properly regarded as an officer within the meaning of Section 10 of the Winding-up Act of 1890. That section runs thus : " Where, in the course of the winding-up of a company under the Companies Acts, it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager, liquidator, or other officer of the company has misapplied or retained, or become liable or accountable for any moneys or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may, on the application of the Official Receiver, or of the liquidator of the company, or of any creditor or contributory of the company, examine into the conduct of such promoter, director, manager, liquidator, or other officer of the company, and compel him to repay any moneys or restore any property so misapplied or retained, or for which he has become liable or accountable, together with interest after such rate as the Court thinks just, or to contribute such sums of money to the assets of the company by way of compensation in respect of such misapplication, retainer, misfeasance, or breach of trust as the Court thinks just."

Now it is urged by Mr. Cohen that the Auditor of a company is not an officer within the meaning of that section. It appears to me that in order to decide that question we must examine and consider what an Auditor is, how he is appointed, by whom he is paid, and what his duties are. This is a company—a banking company—and the Auditor is required to be appointed under the Companies Act of 1879. This Companies Act of 1879 is one of the group of Acts which are usually referred to as the Companies Acts from 1862 down to, I think, 1890. Now Section 7 of this Companies Act of 1879 runs thus :—" Once at the least in every year the accounts of every banking company registered after the passing of this Act as a limited company shall be examined by an Auditor or Auditors, who shall be elected annually by the company in general meeting. A director or officer of the company shall not be capable of being elected Auditor of such company. An Auditor on quitting office shall be re-eligible. If any

casual vacancy occurs in the office of any Auditor, the surviving Auditor or Auditors (if any) may act, but if there is no surviving Auditor, the directors shall forthwith call an extraordinary general meeting for the purpose of supplying the vacancy or vacancies in the Auditorship. Every Auditor shall have a list delivered to him of all books kept by the company, and shall at all reasonable times have access to the books and accounts of the company; and any Auditor may, in relation to such books and accounts, examine the directors or any other officer of the company. Provided that if a banking company has branch banks beyond the limits of Europe, it shall be sufficient if the Auditor is allowed access to such copies of and extracts from the books and accounts of any such branch as may have been transmitted to the head office of the banking company in the United Kingdom. The Auditor or Auditors shall make a report to the members on the accounts examined by him or them, and on every Balance Sheet laid before the company in general meeting during his or their tenure of office; and in every such report shall state whether, in his or their opinion, the Balance Sheet referred to in the report is a full and fair Balance Sheet properly drawn up, so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company, and such report shall be read before the company in general meeting. The remuneration of the Auditor or Auditors shall be fixed by the general meeting appointing such Auditor or Auditors, and shall be paid by the company." And Section 8 says "the Auditors shall sign a Balance Sheet," and so on. Now reading that section alone, it seems impossible to deny that for some purposes and to some extent an Auditor is an officer of the company. He is appointed by the company, he is paid by the company, and his position is described in the section as that of an officer of the company. He is not a servant of the directors. On the contrary, he is appointed by the company to check the directors, and for some purposes, and to some extent, it seems to me quite impossible to say that he is not an officer of the company.

Well, so much for the Act. If we pass to the articles of this particular company, we shall find there are some which are important. On p. 6, Article 2, "Auditors and secretary" (this is the definition clause) "means those respective officers from time to time of the company." Article 73, on p. 23, runs thus: "Every director, Auditor, manager, secretary, and other officer shall be indemnified by the company from all losses and expenses incurred by them respectively in or about the discharge of their respective duties, except such as happen from their own respective wilful acts or defaults." Then Article 107, p. 30, runs thus (this is about the auditing): "The accounts of the company shall be from time to time examined," and so on. And then, 108, "No

person shall be eligible as an Auditor who is not a shareholder of the company, or who is interested otherwise than as a shareholder or customer in any transactions of the company, and no director or officer of the company shall, during his continuance in office, be eligible as an Auditor." Then, "Auditors shall be appointed at the ordinary meetings of the company each year by the shareholders present thereat, and shall only hold their offices until the ordinary meetings in every year after their appointment. Retiring Auditors shall be eligible for re-election. No person, not being a retiring Auditor, shall be eligible to the office of Auditor unless notice of an intention to propose him at an ordinary meeting be given at least fourteen days and not more than one month before the meeting, and a copy of every such notice shall be posted up at the office during the five days next before the meeting. The remuneration of the Auditors shall be determined, and may be from time to time varied by general meetings." Then there is Article 121, on page 33, "Every director, manager, Auditor, trustee, member of a committee, officer, servant, agent, accountant, or other person employed in the business of the company shall, before entering upon his duties, sign a declaration pledging himself to observe a strict secrecy," and so on.

I do not think there is anything else in those articles which is material. I do not know that those articles carry the matter very much further than the section of the Act to which I have alluded, and my observations upon the articles and that Act are those which I have already made, viz., that for some purpose, and to some extent, at all events, an Auditor is an officer appointed by the company, although in no sense a servant of the directors.

Then it is said—it is not denied in truth—but it is said that for all that he is not an officer of the company within the meaning of Section 10. And it is put in this way, that an officer within the meaning of Section 10 is an officer who, in some way or other, has control over the assets of the company. Now it is quite obvious that this section applies to something more than the misapplication of assets. Misapplication or retainer or becoming liable or accountable for the assets is provided for by the first part of the section which I have read; but, in addition to that, there is mention made of misfeasance or breach of trust in relation to the company, and, with reference to that, provision is made not by the words which authorise the Court to compel the person guilty of misfeasance or breach of trust to repay any moneys or restore any property, but to contribute such sums of money to the assets of the company by way of compensation in respect of such mis-

application, retainer, misfeasance, or breach of trust as the Court thinks just.

I know nothing at all about the charge against this Auditor upon the facts, but suppose that an Auditor whose business it is to audit accounts and sign Balance Sheets, knowing perfectly well that that Balance Sheet so signed by him will be acted upon, shows profits properly divisible as dividend, a dividend will be declared; and suppose that he purposely and fraudulently prepares and signs a Balance Sheet showing profits divisible when there are none. It appears to me that that is a distinct misfeasance in that sense within the meaning of that Act, leading to and intending to lead to a misapplication of the assets. Such a misfeasance, I have not the slightest doubt, would be a misfeasance within the meaning of the section. Although that does not show that he is an officer of the company, yet, having regard to the articles of association of this company and the provisions I have just referred to, I do not see how it can be said that, as a matter of law, this gentleman is not an officer of the company and cannot be liable for misfeasance. In my opinion he is an officer, and may be within the misfeasance contemplated by Section 10.

Now, it is said that that is very hard upon persons who are Auditors, and that if they are guilty of negligence, fraud, or misconduct, the proper way is by an action. But suppose an action were brought against an Auditor upon the ground that the accounts had been fraudulently audited, how could that be possibly tried by a jury? It would demand and would necessitate a prolonged investigation of the accounts, and no one who has any experience of trial by jury would for a moment pretend that it could be so tried, and therefore it must be referred to some other tribunal. Therefore, the point made by Mr. Cohen that you are going to deprive him of his constitutional right really does not apply, and it appears to me that the objection fails, and therefore we are not prepared to say, and cannot say, that the Auditor of a company in a case like this is not an officer of the company within Section 10.

Lopes, L.J. : I am of the same opinion. The question is whether an Auditor, such as the Auditor in this case, is an officer within the true meaning of Section 10. I do not propose to read the section again, which has already been read, but it is to be observed in respect of this section that it does not create any new rights, but it gives a very summary mode of procedure in enforcing rights already existing. Now, if it were not for the word "misfeasance" in Section 10, I should not have thought that an Auditor, such as the Auditor in the present case, came within the meaning of that section.

I should have thought that the section, if that word had been absent, was rather directed against those who had to carry out the business and purposes of the company, who had the control over the assets of the company, who had the conduct of the business, and who might have the money or the property of the company in their hands, which they might apply, retain, or restore. But I find the word "misfeasance," and, as I understand the word "misfeasance" in this section, it means a breach of duty. Now, if it means a breach of duty, one can quite understand a breach of duty which might be committed, which might be effected, by an Auditor. For instance, he might, in collusion with his directors, prepare a false account, which would involve a misapplication of the assets. Now, in such a case, it seems to me that that would be one of the mischiefs which this section was intended to prevent. I come, therefore, to the conclusion that an Auditor, such as that of a banking company, is an officer within the meaning of that section. And I am fortified in that view by the words of the section of the Companies Act of 1879, because it seems to me that that section recognises the Auditor of a banking company, and recognises the Auditor of a banking company as an officer. If you look at the subsection, it says: "If any casual vacancy occurs in the office of Auditor"; and throughout, the section seems to contemplate that the Auditor is an officer of the company. That fortifies the view that I have formed with regard to Section 10, and I am also confirmed in that view by the fact that the articles of association of this very banking company recognise the Auditor as an officer. Now, there was a case referred to, which is a case *In re The Liberator Permanent Benefit Building Society*, which came before Mr. Justice Cave and Mr. Justice Collins, and I find it reported in the 71st volume of the *Law Times*, on page 406. That was not a case of an Auditor. That was the case of a solicitor. It was not the case of a banking company, but of a building society. And it is true that Mr. Justice Cave, in the course of his judgment, says: "It seems to me that merely because he was appointed solicitor to the society, without more, the solicitor does not become an officer to the society any more than it has been held that a banker does, if he is appointed banker to the society, or a broker if he is appointed broker to the society, or the Auditor if he is appointed Auditor to the society." I do not think that the attention of Mr. Justice Cave was drawn to the word "misfeasance"; but, however that may have been, that was not a case of an Auditor, but the case of a solicitor, that had been decided; and it may be again said that the section of the Act of 1879 which relates to the Auditor of a banking company, would not relate in the same way to a solicitor, and, for anything I know (I have not been able to find it out), it does not

appear that the articles of association, so far as I can see, recognise the Auditor as an officer. I come, therefore, to the conclusion that the Auditor of this banking company was an officer within the true meaning of Section 10 of the Companies (Winding-up) Act of 1890.

Kay, L.J.: I come to the same conclusion, but I wish to guard myself against being understood to hold that, in every case of a joint-stock company, the Auditor employed by the joint-stock company is an officer of the company. I do not at present hold that opinion; I can quite conceive there may be one or two cases of a joint-stock company who call in an Auditor to make a particular audit, where the Auditor called in could not be properly treated as an officer of the company; but we have got to deal in this case with a joint-stock company—a banking company limited—whose duties, in respect of having their accounts audited, are prescribed by the Act of 1879, to which reference has been made. And it will be observed, on looking at that Act of Parliament, Section 7, that the Auditor is to be appointed by the company in general meeting. The first sub-section of Section 7 says that “Once at least in every year the accounts of every banking company registered after the passing of this Act as a limited liability company shall be examined by an Auditor or Auditors, who shall be elected annually by the company in general meeting.” So that the election is not like the election of the ordinary officers of the society—delegated to the directors of the company, but it is prescribed by statute that there shall, in this case, be an Auditor elected by the company in general meeting. Then I find, turning to the articles of this society, that they recognise distinctly their duty, and by the interpretation clause of their articles they do define expressly that the Auditor of this company shall be an officer of this company. The words have been read, but I will just refer to them again for a moment. The first of the articles is: “Auditors and secretary means those respective officers from time to time of the company.” Then, again, we find in Section 73 a recognition of the fact that Auditors duly appointed by the company are officers of the company; and then come the sections which speak of the duties of Auditors, Section 107 and Section 108; and Section 108 (some comments were made with regard to the words and the language of that section) provides that no director or officer of the company shall, during his continuance in office, be eligible as Auditor. It was said that that shows plainly that an Auditor is not to be an officer of the company but somebody who is not an officer. I do not read it in that sense. That is a mere copy of the language of the Act of 1879, which provides in Section 7, Sub-section 2, that “a director or officer of the company shall not be capable of being elected an Auditor of such company.” Here the Auditor is treated as an officer of the company. They

provide also in their articles that the Auditor shall not hold any other office in the company. At the same time, I take Article 108 not to contradict that which has been said in the earlier part of these articles, that an Auditor of this company is an officer of the company, but merely to provide, as the statute provides, that while he is an Auditor he shall not hold any other office in the company. The object of that section is that he might not hold some other office the duties of which might bias him in his conduct as an Auditor; and, therefore, to prevent the danger of that it is provided by the statute, and repeated by the articles, that he cannot hold at the same time any other office of the company. That seems to me to reconcile these articles with the statute, and, dealing with this particular clause, which is all we have got to consider now, I come to the conclusion that in this case the company in its constitution recognised the necessity of having Auditors duly appointed under the statute of 1879, and made these provisions that Auditors so appointed should be treated by this company as being officers of the company. In the face of that it seems to me quite impossible to hold that Auditors are not officers of the company. Then whether they are officers within Section 10 or not, seems to be almost concluded when you come to the opinion that this company did appoint its Auditors as officers of the company. For, after all, all the section provides is only a convenient mode of dealing with, amongst other things, the misapplication of the funds of the company by its officers. On the other hand, also, for misfeasance (misfeasance other than misapplication of the money of the company which may lead to an injury and damage to the company, and which is to be met, not by replacing the misappropriated funds, but, as the section says, by compensation to the company) the words "misfeasance" and "compensation," as used in that section, seem to me to be clearly correlative; and when that section speaks of the misfeasance of an officer of the company, it must mean, looking to the collocated words, misfeasance other than the misapplication or misappropriation of the funds or property of the company. And to remedy that misfeasance the power which that section gives requires that persons convicted of misfeasance shall make compensation to the company. As has been said by Lindley, L.J., the possibility of misfeasance by an Auditor might produce very considerable damage and injury to the company of which he was Auditor, and in that case it seems to me that he does come within the section, and that as I read the terms of this Section 10 he can be made liable for such misfeasance, and can be obliged to make compensation to the company, and I therefore think that that must be our ruling.

Lindley, L.J.: Now the next question is, What ought to be done with reference to the hearing of this appeal? And it has given us a

great deal of trouble and anxiety to decide what is to be the right manner of dealing with it. We were very much impressed by the observations made by Sir Edward Clarke, that the learned Judge had, apparently, acted upon materials which were not in evidence before him, and which the parties had had no opportunity of answering, or being heard upon, and before making up our minds as to what was to be done we thought it right to communicate with the learned Judge himself to ascertain what the real facts were. Now he has reported to us, as to the observations made by him on pp. 27 and 28 of his printed judgment, that what took place was this—that he went through the books of this company himself, and came to certain conclusions which he desired to have further information upon, and he checked them to verify them. He did that, and then with the consent which we heard of the other day, asked for, and obtained, the assistance of Mr. Bramall and of Mr. Avery, and they prepared things called “schedules,” which I confess I have not examined, and the learned Judge says that those “schedules” consisted substantially of two parts, some central columns which contained only what could be got out of the books of this company, and which were strictly in evidence, and they were accompanied by remarks and observations in other parts, and the documents which were before them; and he informs us that he discarded everything except that which was properly evidence in the case, but that having seen these observations he did not think it fair or right not to inform the parties that he had done so, and that explains this passage in his judgment to which reference has been made.

Now, under these circumstances, we are clearly of opinion that the very last thing we ought to do is to refer this either for a new trial or to an official referee, thereby putting the parties to the expense of going through the whole thing again, unless we are actually driven (when we suggested that course the other day we thought we should be driven) to adopt it, but having received the observations of the learned Judge, we feel that it is our duty to hear the appeal ourselves, putting upon the appellants the ordinary burthen of showing that the decision is wrong, we attending only to what is legitimate evidence in the case. We propose, therefore, to fix a day, say, the 20th May, to hear the appeal in the ordinary course. If it should become necessary in the course of the appeal to adduce further evidence we have ample power to do it, and we shall exercise our own judgment; but, at the same time, it is a course which, we think, we ought not to take unless we are absolutely driven to it.

It was subsequently decided to hold over the appeal until the second day of next sittings.

(*Acct. L.R.*, 1895, p. 72.)

The case of THE LONDON AND GENERAL BANK, LIM.

(Decided before Lords Justices LINDLEY, LOPES, and RIGBY, in the Court of Appeal, on 6th August 1895.)

Held that an Auditor is guilty of Misfeasance who, when dissatisfied with the Accounts of a Company, does not plainly draw attention to the grounds for his dissatisfaction in his Certificate.

JUDGMENT.

Lord Justice Lindley: This is an appeal by Mr. Theobald, one of the Auditors of the London and General Bank, which is being wound up, against an order made by Mr. Justice Vaughan Williams, under Section 10 of the Companies Act 1890. By this order Mr. Theobald and the directors of the bank are declared jointly and severally liable to pay to the Official Receiver of the company two sums of £5,946 12s. od. and £8,486 11s. od., being respectively the amounts of dividends declared and paid by the bank for the years 1890 and 1891, with interest on those sums. The grounds on which this order was made on Mr. Theobald are that these dividends were paid out of capital, and that such payment was made pursuant to resolutions of the shareholders based upon recommendations of the directors of the bank, and upon Balance Sheets prepared and certified by Mr. Theobald, and which did not truly represent the financial position of the company.

Mr. Theobald's appeal was supported by arguments to the effect (1) that Mr. Theobald was not an officer of the company within the meaning of Section 10 of the Winding-up Act 1890; (2) that the Balance Sheets and certificates given by Mr. Theobald were in accordance with the books of the bank, and that Mr. Theobald's duty as Auditor was confined to framing the Balance Sheets, which showed the position of the bank as disclosed by its books; (3) that the dividends in question were not really paid out of capital, and that however imprudent and reckless it may have been to pay them, Mr. Theobald, as Auditor, is not legally responsible for such payment; (4) that even if Mr. Theobald, as Auditor, failed adequately to discharge his duty, and even if the dividends were paid out of capital, his failure to discharge his duty was the remote and not the proximate cause of the non-payment of the dividends, and that he, consequently, is not legally liable to make good the amount so paid; (5) that at any rate the order is wrong in declaring him liable jointly and severally with the directors to repay the dividends in question.

The first of these contentions was argued and decided last April, and the Court then held that an Auditor of a banking company governed by the Companies Act 1879, and by such articles as regulated the present company, was an officer of the company within the meaning of Section 10 of the Winding-up Act 1890, and was liable to have proceedings taken against him under that section. This point, having been thus decided, was, of course, not again raised, and nothing further need be said about it.

It remains, however, to consider what the duties of an Auditor are as respects companies governed by the Companies Act 1879, and by such articles as regulate this particular company. It will be convenient to do this before examining the facts relied upon by the liquidator as making Mr. Theobald liable to make good the dividends which he has been ordered to pay. Section 7 of the Companies Act of 1879, Clauses 1, 5, and 6, are material. "7 (1) Once at the least in every year the accounts of every banking company registered after the passing of this Act as a limited company shall be examined by an Auditor or Auditors, who shall be elected annually by the company in general meeting." Then Clause 5 is :—"Every Auditor shall have a list delivered to him of all books kept by the company, and shall at all reasonable times have access to the books and accounts of the company; and any Auditor may, in relation to such books and accounts, examine the directors or any other officer of the company." Then there is a proviso, which one need not read, about banks beyond the limits of Europe. Then 6 is :—"The Auditor or Auditors shall make a report to the members on the accounts examined by him or them, and on every Balance Sheet laid before the company in general meeting during his or their tenure of office; and in every such report shall state whether, in his or their opinion, the Balance Sheet referred to in the report is a full and fair Balance Sheet properly drawn up, so as to exhibit a true and correct view of the state of the company's affairs, as shown by the books of the company, and such report shall be read before the company in general meeting." Then "7. The remuneration of the Auditor or Auditors shall be fixed by the general meeting appointing such Auditor or Auditors, and shall be paid by the company." It is necessary also to read Articles 106, 107, and 114. Article 106, which is under the head "Accounts," runs thus :—"At every ordinary meeting the directors shall lay before the meeting a Balance Sheet showing the financial state of the company for the previous financial year, duly audited, and every such Balance Sheet shall be accompanied by a report of the directors as to the state and condition of the company, and as to the amount which they recommend to be paid out of the profits

by way of dividend or bonus to the shareholders, after allowing for any interim dividend which the directors may have declared, and any sum which they may have set aside under Article 116 hereof." Then Article 107, which is under the head "Audit," runs thus:—"The accounts of the company shall be from time to time examined and the correctness of the statements shall be from time to time ascertained, by two or more Auditors, in accordance with these presents." Then Article 114, which, I think, is the only further one I need read at this moment, runs thus:—"The Auditors shall be supplied with copies of the statement of accounts intended to be laid before the meeting, and it shall be their duty to examine the same with the accounts and vouchers relating thereto." These are the enactments and regulations which bear directly on the duties of the Auditors, and although Articles 107 and 114 are in terms more explicit than Section 7 of the statute as regards the duty of the Auditors to examine and ascertain the correctness of the statements laid before them, and of the accounts laid before the shareholders, yet it is tolerably plain from the language of Section 7 of the Act, Clause 5, that the articles add little, if anything, to the duties imposed on the Auditors by the statute alone.

In connection with these articles, and in order to save repetition, it should be stated that by the articles of this bank it is the duty of the directors, and not of the Auditors, to recommend to the shareholders the amounts to be appropriated for dividends; and it is the duty of the directors to have proper accounts kept so as to show the true state and position of the company. Lastly, it is for the shareholders, but only on the recommendation of the directors, to declare a dividend.

It is impossible to read Section 7 of the Companies Act 1879 without being struck with the importance of the enactment that the Auditors are to be appointed by the shareholders, and are to report to them directly, and not to, or through, the directors. The object of this enactment is obvious. It evidently is to secure to the shareholders independent and reliable information respecting the true financial position of the company at the time of the audit. The articles of this particular company are even more explicit on this point than the statute itself, and remove any possible ambiguity to which the language of the statute, taken alone, may be open if very narrowly criticised.

It is no part of an Auditor's duty to give advice either to directors or shareholders as to what they ought to do. An Auditor has nothing to do with the prudence or imprudence of making loans with or without security. It is nothing to him whether the business of a company is

being conducted prudently or imprudently, profitably or unprofitably ; it is nothing to him whether dividends are properly or improperly declared, provided he discharges his own duty to the shareholders. His business is to ascertain and state the true financial position of the company at the time of the audit, and his duty is confined to that. But then comes the question : How is he to ascertain such position ? The answer is : By examining the books of the company. But he does not discharge his duty by doing this without inquiry and without taking any trouble to see that the books of the company themselves show the company's true position. He must take reasonable care to ascertain that they do. Unless he does this, his duty will be worse than a farce. Assuming the books to be so kept as to show the true position of the company, the Auditor has to frame a Balance Sheet showing that position according to the books, and to certify that the Balance Sheet presented is correct in that sense. But his first duty is to examine the books, not merely for the purpose of ascertaining what they do show, but also for the purpose of satisfying himself that they show the true financial position of the company. This is quite in accordance with the decision of Mr. Justice Stirling in *The Leeds Estate Company v. Shephard*, in 36 Chancery Division, page 802. An Auditor, however, is not bound to do more than exercise reasonable care and skill in making inquiries and investigations. He is not an insurer ; he does not guarantee that the books do correctly show the true position of the company's affairs ; he does not guarantee that his Balance Sheet is accurate according to the books of the company. If he did he would be responsible for an error on his part, even if he were himself deceived, without any want of reasonable care on his part—say, by the fraudulent concealment of a book from him. His obligation is not so onerous as this.

Such I take to be the duty of the Auditor ; he must be honest—that is, he must not certify what he does not believe to be true, and he must take reasonable care and skill before he believes that what he certifies is true.

What is reasonable care in any particular case must depend upon the circumstances of that case. Where there is nothing to excite suspicion, very little inquiry will be reasonable and sufficient ; and in practice, I believe, business men select a few cases haphazard, see that they are right, and assume that others like them are correct also. Where suspicion is aroused more care is obviously necessary, but still an Auditor is not bound to exercise more than reasonable care and skill even in a case of suspicion ; and he is perfectly justified in acting on the opinion of an expert where special knowledge is required.

Mr. Theobald's evidence satisfies me that he took the same view as myself of his duty in investigating the company's books and preparing his Balance Sheet. He did not content himself with making his Balance Sheet from the books without troubling himself about the truth of what they showed. He checked the cash, examined vouchers for payments, saw that the bills and securities entered in the books were correct, took reasonable care to ascertain their value, and in one case obtained a solicitor's opinion on the validity of an equitable charge. I see no trace whatever of any failure by him in the performance of this part of his duty. It is satisfactory to find that the legal standard of duty is not too high for business purposes, and is recognised as correct by business men.

The Balance Sheet and certificate of February 1892, that is, for the year 1891, was accompanied by a report to the directors of the bank. Taking the Balance Sheet, the certificate, and report together, Mr. Theobald stated to the directors the true financial position of the bank, and if this report had been laid before the shareholders, Mr. Theobald would have completely discharged his duty to them. Unfortunately, however, this report was not laid before the shareholders, and it becomes necessary to consider the legal consequences to Mr. Theobald of this circumstance.

A person whose duty it is to convey information to others does not discharge that duty by simply giving them so much information as is calculated to induce them, or some of them, to ask for more. Information and means of information are by no means equivalent terms. Still, there may be circumstances under which information given in the shape of a printed document circulated amongst a large body of shareholders would by its consequent publicity be very injurious to their interests, and in such a case I am not prepared to say that an Auditor would fail to discharge his duty, if instead of publishing his report in such a way as to ensure publicity, he made a confidential report to the shareholders, and invited their attention to it, and told them where they could see it. The Auditor is to make a report to the shareholders, but the mode of doing so, and the form of the report, are not prescribed. If, therefore, Mr. Theobald had laid before the shareholders the Balance Sheet and the Profit and Loss Account accompanied by a certificate in the form in which he had prepared it, he would perhaps have done enough, under the peculiar circumstances of the case. I feel, however, the great danger of acting on such a principle, and in order not to be misunderstood, I will add that an Auditor who gives shareholders means of information instead of information in respect of a company's financial position does so at his peril, and runs the verv

serious risk of being held, judicially, to have failed to discharge his duty.

In this case I have no hesitation in saying that Mr. Theobald did fail to discharge his duty to the shareholders in certifying and laying before them the Balance Sheet of February 1892, without any reference to the report which he laid before the directors, and with no other warning than is conveyed by the words "The value of the assets as shown on the Balance Sheet is dependent upon realisation." The most important asset on that Balance Sheet is put down as "Loans to customers and other securities, £346,975," and on those a full and detailed report was made to the directors, showing the very unsatisfactory state of these loans and securities, and it is impossible to read the oral evidence, the report of Mr. Balfour and Mr. Brock, dated the 22nd of December 1891, and the report of the Auditor to the directors of the 3rd of February 1892, without coming to the conclusion that the entry of that large sum as a good asset without explanation was unjustifiable. It is a mere truism to say that the value of loans and securities depends upon their realisation. We are told that a statement to that effect is so unusual that the mere presence of those words is enough to excite suspicion. But, as already stated, the duty of an Auditor is to convey information, not to arouse inquiry, and although an Auditor might infer from an unusual statement that something was seriously wrong, it by no means follows that ordinary people would have their suspicions aroused by a similar statement if, as in this case, its language expresses no more than any ordinary person would infer without it.

But Mr. Theobald relies on the fact that he was induced to omit from his certificate all reference to the report which he made to the directors, because Mr. Balfour, the chairman, promised to mention such report in his speech to the shareholders, and he did so. But although Mr. Balfour twice alluded to the report, he did so in such a way as to avoid attracting attention to it. The second time he mentioned it was after a dividend had been declared, and when a motion to re-appoint the Auditors was before the meeting. The truth is that not a word was said to convey to the shareholders the substance of the information contained in the report, or to induce them to ask any question about it. The Balance Sheet and the Profit and Loss Account were true and correct in this sense, that they were in accordance with the books. But they were, nevertheless, entirely misleading, and misrepresented the real position of the company. Under these circumstances, I am compelled to hold that Mr. Theobald failed to discharge his duty to the shareholders with respect to the Balance Sheet and certificate of February 1892. Possibly he did not realise the extent of his duty to the

shareholders as distinguished from the directors, and he, unfortunately, consented to leave the chairman to explain the true state of the company to the shareholders instead of doing so himself. The fact, however, remains, and cannot be got over, that the Balance Sheet and certificate of February 1892 did not show the true position of the company at the end of 1891, and that this was owing to the omission by the Auditor to lay before the shareholders material information which he had obtained in the course of his employment as Auditor of the company, and to which he called the attention of the directors.

But then it is contended that, even if this be so, there was, after all, no payment of a dividend out of capital; and further that, even if there was, still that such payment was not the natural or immediate result of Mr. Theobald's certificate, and of the accounts which he prepared.

Whether the payment was made out of capital or not is a question of fact. It was professedly made out of profits made by the bank by charging its customers with interest and commission on loans and discounts. The books showed such profit, but the question is, where did the money come from with which the dividends were paid? The money came from cash at the bankers or in hand, but this cash could not be properly treated as profit, and the directors and Auditors knew this perfectly well. This part of the case has been most carefully investigated by the learned Judge whose decision we are reviewing, and after attending most attentively to the observations of counsel on the reasonings and conclusions contained in the judgment appealed from, I see no reason whatever for dissenting from them. On the contrary, I entirely agree with him in saying that the profits for the year 1891 never really existed except on paper—that, to use his words, "Whatever may be the right line to draw as to when profit not received may be carried to profit for the purpose of the annual Revenue Account, it is plain that there was no justification for so doing in the present case." The real truth is that the assets of the bank were put down in the Balance Sheet at far too high a figure, and this entry, though not misleading if explained (as it was to the directors), was seriously misleading in the absence of explanation. Mr. Theobald says that he regarded the assets of the bank as only locked up, but his report and the schedule to it go far beyond this. The value of the principal asset depended on the probability of the Balfour group of companies and some of the other large borrowers repaying their loans. They were financing each other, their indebtedness to the bank increased largely during the year, the securities held by the bank for these loans were, to say the least, of very

doubtful character, and yet the total amount due to the bank in respect of these loans is inserted in the Balance Sheet as a good asset without any deduction, and without a word of explanation to the shareholders. We now know that these assets have realised a comparatively small sum, and we were very properly warned against the danger of doing injustice by being wise after the event. But disregarding the result of realisation and attending only to what was known to the Auditors in February 1892, the entry in the Balance Sheet of the sum of £346,975 as a good asset was wholly unjustifiable unless explained.

We are now in a position to understand the true meaning of a passage contained in the Auditors' report to the directors of the 3rd February 1892, and which runs thus: "We cannot conclude without expressing our opinion unhesitatingly that no dividend should be paid this year." I find it impossible to treat this as a statement by the Auditors that there are profits divisible among the shareholders, but that the Auditors cannot recommend a dividend. I can only regard the passage as meaning that there are no funds out of which the dividend can properly be paid, and, therefore, no dividend ought to be paid this year. A dividend of 7 per cent. was, nevertheless, recommended by the directors, and was resolved upon by the shareholders at a meeting furnished with the Balance Sheet and Profit and Loss Account certified by the Auditors, and at which meeting the Auditors were present, but silent. Not a word was said to inform the shareholders of the true state of affairs. It is idle to say that these accounts are so remotely connected with the payment of the dividend as to render the Auditors legally irresponsible for such payment. The Balance Sheet and account certified by the Auditors as showing a profit available for dividend were, in my judgment, not the remote, but the real operating cause of the motion for the payment of the dividend which the directors improperly recommended. The Auditors' account and certificate gave weight to such a recommendation and rendered it acceptable to the meeting. It was wholly unnecessary for the Official Receiver to call a shareholder to say that he was induced by the Auditors' certificate to concur in the resolution to pay a dividend. As to this part of the case, *res ipsa loquitur*.

The point was made that the form of the order was wrong. But there was nothing in this. Mr. Theobald could obviously be sued alone in an action at law for breach of his statutory duty as Auditor, and the measure of damages would be the sum which he has been ordered to pay. Whether a similar action at law could be maintained against him and the directors jointly is more open to question. I am by no

means satisfied that it could not, seeing that the wrongful payment of the dividend was caused by his improper certificate and accounts, and by the use made of them by the directors. But, be this as it may, there was a clear breach of trust by the directors, facilitated, and, indeed, only rendered possible by the Auditor, who failed in discharging his own duty to the shareholders; and I have no doubt that in equity both he and they could be held jointly and severally liable for the misapplication of the company's moneys, which constituted a breach of trust. In respect, therefore, to the sum of £8,486 11s. wrongfully paid as dividend in 1892 in respect of the alleged profits made in 1891, the appeal in my opinion fails.

I pass now to the accounts and Balance Sheet prepared by the Auditors in February 1891, and showing the state of affairs in 1890. A profit for that year was shown, and a dividend of £5,946 12s. was declared and paid, and Mr. Theobald has been held liable for this sum also. I agree with Mr. Justice Vaughan Williams in holding that the dividend for 1890 was in fact improperly declared and paid. But the evidence that Mr. Theobald was guilty of any breach of duty in certifying the accounts in February 1891 is far less cogent than that which presses so heavily against him with reference to the accounts of February 1892. The truth is that the conviction that the bank's affairs were every year getting worse and worse grew upon him year by year. This state of things was shown by the decrease of its reserve capital, and the increase of its loans to customers. But the loans to customers were, speaking roughly, £100,000 less at the end of the year 1890 than at the end of 1891, and seeing that the accounts prepared by the Auditors did accurately represent the position of the company as shown by the books, and that it is not proved that Mr. Theobald really knew, or ought then to have known, that the position of the bank was not correctly shown by the books, I think Mr. Justice Vaughan Williams has gone too far in holding Mr. Theobald liable for this sum. The reasons which induced the learned Judge to decide that Mr. Theobald was not liable for the dividends paid in 1889 and 1890 appear to me to apply also to the dividends paid in 1891 in respect of the profits of 1890. No doubt the change made by the Auditors in 1886 in the form of the certificate they gave is really significant, and, unexplained, leads to the inference that the Auditors did not believe that the books of the company and the Balance Sheet prepared from them correctly showed the position of the bank. But Mr. Theobald's evidence does, in my opinion, show that in February 1891 matters were not known or believed to be so bad as to lead him to the conclusion that there were then no profits out of which a dividend could properly be paid. It is true that the position

of the bank was very unsatisfactory in 1890, and the Auditors knew it to be so. This, however, appeared from the Balance Sheet and accounts which they laid before the shareholders. It is known now that the assets were put down at too high a figure; but it is not proved that the Auditors knew it or ought to have known it. The Balfour group of companies, though dependent upon each other, were by no means in so tottering a state as they were a year later. Mr. Wilkinson's debt was still treated by the directors as bearing interest and as a good, or at all events not a bad, debt. Mr. Benham's debt was unsatisfactory, but the Auditors can hardly be blamed for treating it as good, having regard to the solicitor's statement as to the security held for it. This part of the case is very near the line, but having carefully considered it, I do not think that the evidence is sufficiently strong to establish a case of misfeasance on the part of Mr. Theobald in February 1891. I am not satisfied that he was then guilty of more than an excusable error of judgment; although now that all the facts are known the error is seen to have been very serious in its consequences. As to the sum of £5,946 12s. od., therefore, the appeal must be allowed. As regards costs, Mr. Theobald's appeal has resulted in reducing the sum for which he has been held liable; but, in other respects, and as regards his main contention, it has failed. Under these circumstances he ought not to receive or pay any costs of the appeal, and the only order as to costs will be that the Official Receiver be paid his costs out of the assets of the company.

Lord Justice Lopes has read and considered this judgment, and concurs in it.

Lord Justice Rigby: I have had the advantage of reading and considering the judgment just delivered by Lord Justice Lindley, and I might have confined myself to saying I concur in it, but as I have gone carefully into the evidence as against the appellant, I think that I shall do well to show how I have come to the conclusion on which my judgment is founded. I shall not attempt to repeat all that is contained in Lord Justice Lindley's judgment. Where no reference is made to a particular topic it must be taken that I have nothing to add, though I do not wish to detract from anything said. The appeal is against that part of the order of the 20th December 1894 of Mr. Justice Vaughan Williams, which finds Mr. Theobald liable as one of the Auditors of the London and General Bank, Lim., to make good to the assets of the company, jointly with other persons, and severally, the amount with interest from the date of the order of two sums, £6,768 6s. 9d. and £9,328 17s. 4d., being the dividends with

interest thereon down to the date of the order recommended by the directors and declared by meetings of the company in the years 1891 and 1892 for the years 1890 and 1891. I have not taken the same figures as Lord Justice Lindley did, because there has been added to the dividends the amount of interest down to the date of the order. I think it will be the exact figure.

The order was made on a summons taken out by the liquidator of the company in the matter of the Companies Acts and in the matter of the bank, asking, so far as is material for the present appeal, for a declaration of the joint and several liability of the directors and Auditors of the company on the ground that the dividends before mentioned were not paid out of profits but out of capital, and so far as the Auditors were concerned on the ground that they certified and reported that the Balance Sheets which were laid before the company at the said meetings purported to show profits in excess of the sum paid as dividends. I understand the application to have been in substance an application against the Auditors as officers of the company under the 10th Section of the Act of 1890 to compel them to contribute to the assets of the company, by way of compensation for their misfeasance, such sums as the Court may think just.

The main issues, therefore, seem to be whether the Auditors have been guilty of any misfeasance in relation to the company; whether the misfeasance has occasioned loss to the company for which compensation ought to be directed to be made. This will involve the question whether the dividends were, in fact, paid not out of profits, but out of capital, and whether such payment was the fault of the Auditor. Then there will be the question of the amount of compensation which ought to be directed. To determine the first question, I think it will be necessary to consider in some detail the position and duties of the Auditors, what they ought to have done, and what they have done. Then I refer to Sub-section 6 of Section 7 of the Companies Act of 1879, and to those articles of association which have been referred to by Lord Justice Lindley. I do not think it necessary here to read them out. The articles of association cannot absolve the Auditors from any obligation imposed upon them by the statute, and it may be that they do not in this case impose any greater obligations as to the Balance Sheet, though they make it clear that similar obligations extend to all accounts placed before the company, including Profit and Loss Account as well as the Balance Sheet. Under the statute, the members of the company are entitled to have the safeguard of an expression of opinion of the Auditors to the effect, first, that the Balance Sheet is a full and fair Balance Sheet; and, secondly, that it, the Balance Sheet, is properly

drawn up so as to exhibit a true and correct view of the state of the company's affairs. The words "as shown by the books of the company" seem to me to be introduced to relieve the Auditors from any responsibility as to affairs of the company kept out of the books and concealed from them, but not to confine it to a mere statement of the correspondence of the Balance Sheet with the entries in the books. Now, a full and fair Balance Sheet must be such a Balance Sheet as to convey a truthful statement as to the company's position. It must not conceal any known cause of weakness in the financial position, or suggest anything which cannot be supported as fairly correct in a business point of view. The provision as to the Balance Sheet being properly drawn up so as to exhibit a correct view of the state of the company's affairs is taken from, though it does not go quite so far as Article 94, Table A, of the schedule to the Companies Act of 1862. Treated as an addition to the requisition of a full and fair Balance Sheet, it may not be easy to define the full extent of the obligation which it imposes, nor is it necessary to do so in this case, for it certainly requires, as will hereafter appear, a more detailed statement of facts, or a more detailed explanation of the affairs of the bank, than is contained in any of the Balance Sheets of this company.

It will be important to see what information the Auditors actually acquired as to the business of the company, and the way in which they reported upon the successive Balance Sheets. Mr. Theobald and Mr. Timms were Auditors of the bank from its incorporation in 1882, and they made the audit for successive years down to and including the audit for 1891.

The reports of the Auditors to the members always took the form of a certificate or memorandum written on the Balance Sheet for the year. Their reports on the accounts for the years 1882 and 1883 contained a statement to the effect that in their opinion the Balance Sheet exhibited a true and correct view of the position of the bank. In their report on the accounts of 1885 a somewhat less emphatic statement to the same effect appears, but in the subsequent report no such statement is to be found. In a report to the directors dated the 11th February 1886, which refers to the accounts for 1885, Mr. Theobald, after noticing that the first-class investments, kept by bankers for quick realisation in case of need, stood at a considerably reduced sum, and that more than the whole capital of the company was invested in four accounts, viz., the accounts of the Liberator, the Lands Allotment Company, the House and Land Company, and the Building Estates Company, and that these investments could not be easily realised in critical times,

proceeds to say—"You are doubtless aware that it is a rule with bankers to have at hand in cash or easily realisable securities an amount equal to at least one-third of the customers' current accounts. Considering the whole amount of uncalled capital, I consider that in this case the proportion is scarcely sufficient." There can be no doubt that even at this time Mr. Theobald was aware that the state of affairs of the bank was unsatisfactory in the important points of lock-up of capital and consequent deficiency of realisable securities. At this date the cash in hand appeared to be £28,000—I only give the round figures—and the easily realisable securities were worth £12,600, making together £41,000 odd, while the current accounts and deposit accounts of customers together reached £107,000. I have not been able to distinguish the separate amounts of current and deposit accounts at that time. In the Balance Sheet for 1891, more particularly dealt with hereafter, the cash had fallen to £25,000, and the easily realisable securities to £7,820, making together £32,000 odd; hardly more than one-sixth of the sum due to customers on current accounts alone, which had increased to £189,000 odd, the amount due on current and deposit accounts taken together being £282,000. No other report of the Auditors to the directors is put in evidence until that of 1892 as to the accounts of 1891. The report of the Auditors to the members on the accounts for 1886 to 1890, both inclusive, are simply to the effect that the cash and bills receivable are correct, that securities had been produced for the investments and loans (no information being given as to the securities so produced), and that the Balance Sheet is a correct summary of the accounts recorded in the books. In the last-mentioned report is contained for the first time a statement, "The value of the assets as shown on the Balance Sheet is dependent on realisation."

Great stress has been laid on this by counsel for the appellants. They argue that it was sufficient to put members upon inquiry, and that from the course taken at the trial they were debarred from giving the evidence of experts as to the importance and signification of this. I may at once say that it was the duty of the Auditors to convey in direct and express terms to the members any information which they thought proper to be communicated, that the words of the statement are perfectly clear in their meaning, but also entirely unimportant, amounting to a mere truism, and that no evidence of experts would have been of the slightest use for the purpose of giving them a greater importance or signification than they possessed in themselves, even if such evidence were admissible. To me it appears that all the reports from 1886 onwards were imperfect, and that the Auditors in giving reports in such form failed entirely to fulfil the statutory duties imposed upon

them. Counsel for the appellants argued that such a failure would not amount to misfeasance but only to negligence, and that the appellant is not charged by the summons with negligence, but I cannot admit the cogency of this argument. The reports were made in order to fulfil the statutory obligation, and to be read to the meetings in accordance with the statute. Mr. Theobald, with reference to this matter, says at page 74 of the evidence, "My certificate means the same as the Act." Then he is asked, "Do you say you could have given the certificate required by the Act of 1891?" (I think that question must have been meant and understood to mean, "Could you have given the certificate for 1891 required by the Act?") "(A) Yes, certainly. (Q) Then why did you not do so? (A) Because I was not aware that it was considered necessary for me to give the certificate either in the words of the Act or not at all." Mr. Theobald's interpretation of his own certificate cannot be received either in his favour or against him, and we should not unduly press against him apparent admissions made in the course of a very trying cross-examination. But this evidence of his does, I think, go so far as to show that the certificates were in fact given as reports under the Act, and independent of that evidence I think there can be no doubt that they were intended to be and were received and acted upon as reports under the Act.

I consider the giving of the certificates (assuming them to be to the knowledge of the Auditors misleading certificates, a question which I shall deal with separately) to be a misfeasance within the meaning of Section 10 of the Act of 1890, and not a mere act of negligence; and that this was a fair meaning of the charge contained in the summons I can have no doubt, having regard to the terms of the certificates given and the explanations of Mr. Theobald himself, that there was a strong and growing feeling of dissatisfaction in the mind of Mr. Theobald at the state of the affairs of the bank as shown by the books, and I find no sufficient communication of the facts causing this dissatisfaction in the reports. The Balance Sheets when examined do not in my opinion fulfil the statutory requirements of being full and fair Balance Sheets, and they are not properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company. To establish this, I think it necessary to give a short summary of the evidence, as to the years 1889, 1890, and 1891, the only years as to which we have sufficient evidence to be able to arrive at definite conclusions. From the tables set out at page 7 of the Official Receiver's report it appears that during the years 1889, 1890, and 1891 the greater part of the business of the bank consisted in making loans to and discounting bills for a group of companies, nine in number, conveniently referred to as the Balfour group, or the Balfour

companies. Loans were also made or discounting facilities afforded to other companies allied to the Balfour companies, to certain directors of the bank, and customers, including Wilkinson and Benham, who are named in the table, by reason of special considerations affecting their accounts. These accounts of allied companies and the persons last mentioned are for convenience hereinafter referred to as "the special accounts."

The balance due from the Balfour companies at the end of the years 1889, 1890, and 1891 were, for 1889 £119,000, for 1890 £218,000, and for 1891 £308,000. Corresponding balances in the "special accounts" were, for 1889 £77,000, for 1890 £112,000, for 1891 £121,000, the aggregate balances from the Balfour companies and on the special accounts being for 1889 £196,000, for 1890 £321,000, for 1891 £429,000. The corresponding balances due from all other customers and persons were, for 1889 £135,000, for 1890 £103,000, for 1891 £100,000. Roughly speaking, the proportion of what may be called the outside business to that with the Balfour companies and on the special accounts was, at the end of 1889 two-thirds, at the end of 1890 one-third, and at the end of 1891 one-fourth. The paid-up capital increased in 1890 by about £76,000, and in 1891 by about £43,000, or altogether £120,000, but the whole of this, and considerably more than £100,000 in addition, had been absorbed into the accounts of the Balfour companies and the special accounts.

It has already been pointed out that the amount of cash and easily realisable securities at the end of 1891 was hardly more than one-sixth of the amount due to customers on current accounts, or about one-half of what Mr. Theobald had in 1886 pointed out to be required according to the usual practice of bankers.

These figures show an alarming absorption during the three years of the available assets of the company in advances to the Balfour companies and on the special accounts, and a perilous diminution of easily realisable assets. As is usual with banking companies, profits alleged to have been earned by the bank consisted, with unsubstantial exceptions, of interest on loans, discounting of bills, and commissions.

The gross profits entered in the books as having been earned from the Balfour companies, between the incorporation of the bank and the end of 1891, amounted to upwards of £84,000. The amount distributed in dividends during the same period was upwards of £58,000 and the amount carried to reserve fund £13,000. I include there £3,000 carried to reserve fund in accordance with the report on the accounts of 1891, making together £71,000.

The reserve fund, however, was not required by the articles of association to be kept separate, and was not kept separate from the general funds of the bank. It was employed in the bank's business, quite rightly, no doubt.

Subject to an argument as to appropriation of payments dealt with hereafter, the profits supposed to have been earned from the Balfour companies were not actually paid, but they were only debited in the accounts current of the different companies, and, speaking generally, the moneys owing by the different companies went on increasing from year to year. It is evident that, unless these profits could be fairly treated as not only earned but payable within a reasonable time, there would at the end of 1891 be no profits out of which a dividend could be paid, but, on the contrary, a large deficiency.

The learned Judge, after a careful consideration and investigation of the evidence before him, has found, as a fact, that the credits of these companies at the end of each year were generally credits created temporarily for the purpose of audit, and that such credits, in the majority of cases, were created either by the discounting of bills of companies like Hobbs & Co., which bills constituted a mere paper asset, or by loans direct or indirect from the bank itself, the bulk of which were ill-secured.

I see no reason to differ from this conclusion, but it is a conclusion arrived at to an important extent from comparing the books of the bank with the books of other companies of the Balfour group to which the Auditors had no access, and it is only to the extent to which it is founded on entries in the books of the bank itself that it can be used for the purpose of charging the appellant with knowledge of the facts, though it is very important on the question whether the dividends were really paid out of capital or not. The books themselves show that in many instances the accounts were put in credit in the manner described by the learned Judge, but in other cases, and especially with reference to the indirect loans, that is to say, loans made by the bank to one of the companies out of which that company made an advance to another of the group for the purpose of putting the accounts of the latter in credit at the end of the year, the Auditors would have no sufficient means of tracing the transactions.

Having made these general observations I will go on to examine more completely the important case of the accounts for the year 1891. For that purpose, as being more fair to the Auditors, I will assume without at all deciding that, down to the end of 1890, no knowledge that the former Balance Sheets were misleading has been brought home to the

Auditors, and will endeavour to ascertain what additional information the Auditors acquired during the audit for 1891. In the year 1891 the indebtedness of the Balfour companies to the bank as appearing by the bank books was increased by the sum of between £89,000 and £90,000 without any additional securities of importance being given, though, no doubt, to a considerable but unascertained extent money was expended on buildings already charged to the bank, which would make the property charged, though not necessarily the charges in favour of the bank, more valuable.

The securities consisted in the main of charges on buildings being constructed under building agreements, on which large sums had already been charged in priority to the bank. The buildings were unfinished, and required further expenditure of very large sums before they could advantageously be disposed of, and in my judgment there was abundant evidence to show that these securities of the bank were very insufficient, and not realisable at all without the expenditure of further money, which the bank was unable to advance. The sums due on the special accounts had increased from £102,000 to £121,000, that is to say, between £18,000 and £19,000. With regard to these special accounts, I do not think it necessary to go in detail through the list, but I find that the Auditors comment very unfavourably on the security for the following debts:—That of William Blewitt for £7,849; that of Blewitt and Balfour for £2,148; and that of Balfour for £12,000. I think, however, that they may have considered the personal security in these cases sufficient, and I do not found anything on those cases. Wilkinson, at the end of 1890, was indebted to the bank in the sum of £24,000 practically unsecured. Mr. Theobald complained about interest being debited, on the ground that the directors had then more definite information as to the security. This was going through the audit for 1890. The fact is that the security consisted of debentures of a tramway company whose tramway was never built. Interest accordingly ceased to be debited to this account in March 1891. When Mr. Theobald was pressed to explain why the full sum was returned as an asset, he replied that it would have to be provided for out of the reserve fund. He further explained that he thought the account wanted watching, but that it was likely to turn out all right. In examination before the Judge with reference to this debt, he said that he had conferred with the manager, who knew all about the circumstances. "First of all," says he, "I suggested the whole should be written off, but afterwards, Mr. Brock, I think it was, sent for Mr. Blewitt. We had a very serious conference about it, and they convinced me that the time had not come to do that (write off the whole), and they might yet

get the whole of the amount back, but I thought it was not wise to charge interest."

This, I think, falls very far indeed short of showing that the Auditor believed, or could have believed, that the debt was a good debt, though it might have justified the carrying of it to a Suspense Account, instead of writing it off as bad. The importance of the case depends upon the fact that if the debt had not been entered in the Balance Sheet as a good debt, there would have been no profit at all to show for the year 1891. At the end of 1891, Mr. Wilkinson's debt, which had arisen from discounting bills, all of which would appear by the dates to have been dishonoured, was reduced to £16,000 on account of discount by a loan of £10,000, but the indebtedness remained unaffected. With regard to Benham's debt, which increased in the year 1891 from £31,635 to £47,745, it was proved that in 1891 Mr. Theobald refused to pass the security for another year, and, to satisfy him, a letter purporting to come from Benham's solicitor, Mr. Waring, containing an undertaking to pay off £15,000 within a week, was produced. He had also been told, during the audit for 1890, that there was a security under a supposed will which had not been proved, and that they expected to get the will proved very soon. During the audit for 1891 he ascertained that the debt had increased from £31,000 to £47,000, that the £15,000 promised to be repaid had not been repaid, and that the alleged will had not been proved—indeed, it turned out afterwards that such a will never existed. The explanation of Mr. Theobald, that he trusted to the solicitor seeing that the security was all right, is not, under the circumstances altogether satisfactory, but I think it is safer to allow Mr. Theobald the benefit of the defence, though his own report sufficiently shows that he was not himself thoroughly satisfied. I wish to make it plain, so far as I can, that I am only relying on matters which Mr. Theobald ought to have known and must be presumed to have known. The debt of £7,300 from the Medway Portland Cement Company had, like Wilkinson's, ceased to be charged with interest, and could not properly have been treated as a fund for the payment of dividend. With reference to that of the Public Works Company, Lim., amounting to £8,105, the Auditors, in their schedule to their report to the directors, say this—"The realisation of this is very doubtful." There could, therefore, be no justification for treating this as a fund for payment of dividend. Whilst Mr. Theobald was engaged upon the audit of the accounts for 1891, or previously, a report of Messrs. Balfour and Brock, dated 22nd of December 1891, was produced to him as to the way of putting into credit current accounts of Hobbs & Co., Lim., George Newman & Co., Lim., the London, Edinburgh, and Glasgow Insurance Co., and C. H. Wilkinson, by loans from the bank. With

reference to Mr. Wilkinson's account, the proposal "that the overdraft should be made in part by a loan and in part by fresh acceptances of both secured as may be arranged, we think the further loan should be £10,000 on loan and £15,000 on bills." The loan was made, and, apparently, £16,000 was left on security of acceptances, but it does not appear that any security was then arranged for or given, or that Mr. Theobald investigated this matter. Attention was, therefore, called in this particular case to the mode in which the accounts were put in credit as found by the learned Judge. Several facts which appear to me to be most material with reference to the debt of 1891 are to be gathered from the text of the report. I have dealt, to a certain extent, with the schedule in the remarks I have previously made, but as to the text of the report of the Auditors of February 1892, almost every sentence is full of serious meaning. In it they state "that they are unable to give a more satisfactory certificate than the one set forth," which is a mere statement that the Balance Sheet is a correct summary of the accounts as recorded in the books, followed by a statement that the value of the assets as shown on the Balance Sheet is dependent upon realisation, which I have already commented upon, an important sentence: "On this subject we have reported specifically to the board." This may mean they have reported as to the value of the assets, or as to their realisation, or (as I think is the true construction) as to both. The Auditors were induced to withdraw this sentence, which, though it would have given no information of the slightest value to the members, yet would have been calculated to put them upon inquiry. They go on:—"We are not qualified, nor is it the province of the Auditors, to estimate with exactitude the value of the securities." The words "with exactitude" seem to me to be emphatic, and to point out that they had, as appears by the report, made a general estimate of the securities, which was very unfavourable. They say:—"Nevertheless, we feel it our duty to send you herewith a schedule of the securities amounting to £487,000, which we desire should have the special and very serious consideration of the directors."

In the £487,000 are included every one of the sums owing by the Balfour companies and on the special accounts, and nearly £60,000 more out of the £100,000 owing by other customers of the bank. Auditors who feel it their duty to call the special and very serious consideration of their directors to £487,000 out of a total of £530,000 of the debts due to the bank must indeed have arrived at the opinion that the state of affairs of the company was critical and dangerous, but, as will appear, Mr. Theobald does not deny this, though he attempts, unsuccessfully I think, to explain it away by saying that all his anxiety arose from the fact of the assets being locked up. Further on in the

report the Auditors say, "The gravity of the situation is enhanced by the fact, as we believe it to be, that the board is in many cases powerless to decline further help because they are powerless to realise." This appears to me to be a very just but a very serious statement. The Balfour companies were indeed so much bound up with one another by a system of inter-financing, and some of them had committed themselves so deeply in the building schemes of Hobbs & Co., Newman & Co., and others, that they would only be kept going in the future as they had been in the past by continued advances from the funds of the bank. The last quoted extract from the report seems to me to show that the Auditors fully appreciated this view of the state of affairs of the company. They continue as follows:—"We beg also respectfully to point out that the quarters from which the bank obtains by far the larger proportion of its business"—meaning, I conclude, the Balfour companies, and some of the special accounts—"are such that the constitution of the board must make it difficult, if not impossible, to obtain a sufficiently independent judgment upon many vital questions which have to be decided in its management." No doubt this refers to the fact that some members of the board of the bank, the financing company, were members also of the board of different Balfour companies requiring advances, and the difficulty arising from this is obvious and serious. Then follows a sentence which forms an appropriate ending to such a report: "We cannot conclude without expressing the opinion unhesitatingly that no dividend should be paid this year." The Auditors were, unfortunately, persuaded by Mr. Balfour, assisted by Mr. Brock, to strike out this clause, I believe, before the report reached the hands of the other directors of the bank. Mr. Theobald explains this by saying that he came to the conclusion that it was beyond the province of the Auditors to express an opinion as to the policy of declaring a dividend, and if that were all, I should be disposed to agree with him. It is no part of the Auditor's duty to consider what is good or what is bad policy. They have only to examine into facts and see that the members have their opinion as to the Balance Sheet showing the state of affairs of the company. But the context seems to oblige me to read the excised sentence as meaning not that it was impolitic, but that it would be improper, having regard to the state of affairs of the company, to declare a dividend. Having regard to the explanations given by Mr. Theobald in his evidence, I think the postscript to this report very significant. It runs thus: "We do not wish it to be understood that we consider all the accounts in the schedule are unsecured, but as a whole the capital therein represented is locked up." That is the defence, that all their alarm arose from the capital being locked up. This is not, I think, the language that would have been used if the Auditors had thought that the only mischief was in the locking-up, and an examination

of the schedule to my mind confirms this conclusion. To a great extent the memoranda in the schedule explain themselves, and I have already dealt with many of the items. The accounts of each one of the Balfour companies is referred to in such a way as to show the unsatisfactory state of the securities. Mr. Theobald now says that he had no doubt as to the solvency of any of the Balfour companies, and in a certain sense I am ready to believe this; that is to say, he thought that if they continued to be financed in the future as they had been in the past, and so were enabled to complete the buildings which had been commenced, they might ultimately be able to repay the advances to them with interest and commission. But this is not the meaning of solvency in a legal or business sense, and it is quite plain that Mr. Theobald knew perfectly well that some at least of these companies were, and were likely to remain for an indefinite period, unable to meet their liabilities as they became due. In no other way can the memoranda as to the want of security, or the defective nature of the securities, of the several Balfour companies be explained. Similar observations apply to the memoranda as to the special accounts. Notwithstanding this report, every item of the £487,000 was entered as a good debt in the Balance Sheet for 1891. No valuation was made of any one of the debts, or of the securities for them. If any such valuation had, in fact, been made, I think it plain that there could have been no profit shown for the year. Mr. Theobald gave evidence several times over to the effect that whilst he was engaged in the audit for 1891 he felt that it was a very important crisis in the bank's affairs, and that if they could only get over the next month or so they would save it. His explanation of his withdrawal of the words in the proposed report to the members is that on this point he had reported specifically to the board. In explanation he gave, among other carefully prepared and considered reasons, the following: That "Mr. Balfour was so thoroughly aroused to the necessity for taking the affairs of the bank resolutely in hand as to lead me to believe that he would do so, and, being a man of great financial resource, he would be able to save the bank"; and that Mr. Balfour also spoke of an amalgamation. "Mr. Balfour said that, while doing this, he would confer with me continuously, and that no interim dividend should be paid without consultation with me." The first intimation received of payment of the interim dividend was an announcement in the Press of an interim dividend for 1892, for which it is not suggested Mr. Theobald was in any way liable. This would have given twelve months to work, during which time it would have been quite possible for Mr. Balfour to obtain very large repayments from the borrowing companies with which he was connected, and thus for the bank to be saved. That is a very important point to make.

In another place he says, "My main point is this, that the bank could be saved if many of these accounts were collected. Mr. Balfour had absolute power over most of these companies, and he was so thoroughly alarmed that I quite believed that if we could only tide over that period he would use his influence over other companies to bring the money into the bank. I quite imagined he would do that, even if it meant that some of the other companies would have to go to the wall." What becomes of his statement that he thought the companies were solvent? He says it is a critical time; if you can tide over the next month or two—as to which he never expresses an opinion—if you can do that, then the resources of Mr. Balfour are so great, his influence with the other companies so great, that it is quite possible he may collect a number of the accounts, even if the other companies have got to go to the wall. I think it is impossible to avoid the conclusion that Mr. Theobald, when about to make his report on the accounts of 1891, was thoroughly alarmed at the critical position of the bank, as he thought it more than likely the bank would not tide over another month or two, but that if it did, it could only be saved by extraordinary exertions on Mr. Balfour's part, and that in the process some of the other Balfour companies might have to go to the wall. He represents Mr. Balfour as fully sharing his alarm. If we turn to the Balance Sheet to see whether the state of the company's affairs, as apprehended by Mr. Theobald, was in any way indicated therein, we shall, I think, be obliged to answer the question in the negative.

The liabilities appear to be sufficiently set forth. It is the statement of the assets which most calls for criticism. The cash at the bank was correctly stated, and so are the bills receivable, though the amount of £180,000 there appears only to have been arrived at by transferring £58,000 on December 31 1891, from bills receivable to a Loan Account for unpaid expenses. Disregarding the small item for stamps, the only other items on the credit side are as follows:—"Investments including reserve fund"—the reserve fund at that time was £10,000—"2¾ per cent. Consols and Prescott and Arizona Railway bonds, £7,820." That could not be the investments which included the reserve fund of £10,000. "Loans to customers and other securities, £346,000." In the two items, bills receivable and loans to customers and other securities, are, as above pointed out, included the whole of the sums, amounting to £487,000, the subject of the report of the Auditors to the directors, at their full value. This item, loans to customers and other securities, is, of course, altogether inaccurate and may be very misleading. What the £346,000 really consists of is "loans to customers partly secured," which is a very different matter. It would be open to any ordinary reader of the Balance Sheet to suppose that there were securities to an

indefinite amount apart from loans to customers, and available to meet moneys due on the current accounts of customers. I am at a loss to understand for what purpose this item could have been so entered. It was not through inadvertence, for it was a correction of a still more misleading entry occurring in former Balance Sheets. It was suggested that such an item frequently appears in Balance Sheets. It may be so for anything I know, but it is none the less improper in the particular Balance Sheet which we have to consider. In short, the Balance Sheet, as it stands, would have given no hint to any ordinary reader of the critical position arising either from the locking-up of capital or from the doubtful nature of many of the debts entered at their full value. In reporting this Balance Sheet without explanation, the Auditors were, in my judgment, guilty of a misfeasance within the meaning of the 10th Section of the Act of 1890, as charged in the summons, and were in this case, at any rate, thoroughly alive to the unsatisfactory state of the affairs of the bank. They could not but be aware that the Balance Sheet was not properly drawn up so as to show the state of the affairs of the bank as shown by the books. The next question is whether the misfeasance was the cause of loss to the company. On examination of the evidence there set forth, I should be led to the conclusion that the Auditors did know that a dividend could not properly be paid out of profits.

See how the figures stand from another point of view. The Profit and Loss Account shows a gross profit of £24,000. After making provision for bad and doubtful debts, and after deduction of £6,600 for expenses of management and other charges, there is carried over to the Balance Sheet a net profit of £18,000 odd, out of which there had already been applied £6,000 and more in payment of an interim dividend, leaving a balance of between £11,000 and £12,000 and nothing more. £3,000 of that was to be carried to reserve; so you have only about between £8,000 and £9,000, according to the books, for dividend. But of the gross profits for the year 1891 shown by the books, £16,788 were book entries debited to the Balfour companies, £2,462 a book entry debited to Benham's account, and £275 a book entry debited to Wilkinson's account. That, of course, was in the early part of the year, Wilkinson's account being treated as a debit. Assuming all the Balfour companies, and Benham and Wilkinson, to have been able to pay the whole sums due from them, except the amounts debited in 1891 for interest and commission, not only the profits available for dividend would be swept away, but of the reserve fund itself little or nothing would be left. Such an assumption, however, in my judgment, would have been extravagantly favourable to the Auditors, and it only required that one of the debts owing by Mr. Wilkinson

(I leave out Benham because I do not want to found on Benham any charge against Mr. Theobald), or almost any one of the Balfour companies should turn out to be bad, it would exhaust everything belonging to the bank which was not capital. It turned out that each of the Balfour companies, as well as Wilkinson and Benham, as well as other debtors of the bank, were insolvent. In my judgment it is established that the bank had no funds out of which the dividends could in any point of view be properly paid. I think the Auditors might well be held to have known, but I do not rely upon that conclusion in my judgment; what I do rely upon is that the Auditors must have known and did know that the Balance Sheet was not properly drawn up so as to show the state of affairs, and that was a misfeasance. If they were guilty of misfeasance in relation to the company, they must be responsible for the consequences of such misfeasance, whether they had arrived at the conclusion that the dividend if paid at all would be payable out of capital or not. That dividends were, in fact, paid out of capital cannot, I think, be doubted. It was argued that before the stoppage of the bank the profits entered in the 1891 Balance Sheet were, in fact, paid by appropriation of moneys paid into current accounts. This would not apply to a case like Wilkinson's, where there was no current account, but in my judgment the rule in *Clayton's* case has no sort of application under the circumstances. If it had, a bank might always pay profits by mere book entries, though the customers against whom interest and commission were charged might all be hopelessly insolvent. Was, then, the loss occasioned by the misfeasance of the Auditors? It has been argued that the payment of the dividend was not the proximate result of the Auditors' report, as the recommendation of the directors and the vote of the meeting had to intervene. This appears to me to misrepresent the true state of things. The report of the Auditors was a continuing representation, made indeed before, but in law and in good sense to be treated as repeated after, the recommendation of the directors. It was perfectly well known to Mr. Theobald (at any rate at the meeting where he was present and heard the reading of the report recommending a dividend, and the speech of Mr. Balfour) that this report was intended to be relied upon as justifying the recommendation and as an invitation to vote the dividend. How far the judgment should go against the appellant has given me considerable difficulty. A great deal of the reasoning which has led me to hold that their reporting on the accounts of 1891 is a misfeasance in relation to the company applies only to the case of that report. The learned Judge has held Mr. Theobald liable not only for the 1891, but also for the 1890, dividend. I am far from saying that he is clearly wrong, but I cannot satisfy myself that he is clearly right. In the case of the 1890 dividend it

cannot, on the evidence, be made out to my full satisfaction that the Auditors knew the Balance Sheet to be substantially misleading, and I think it safer to confine the order to the dividend in respect of 1891.

Lord Justice Lindley : The order will stand as to one dividend with interest, but not as to the other.

(*Acct. L.R.*, 1895, p. 173.)

The case of THE KINGSTON COTTON MILL COMPANY, LIM.

(Decided before Lord HERSCHELL and Lords Justices A. L. SMITH and RIGBY, in the Court of Appeal, on November 22 1895.)

Held that the Auditor of a Company under Articles similar to "Table A" is an "Officer" of the Company.

This was an appeal from a decision of Mr. Justice Vaughan Williams, reported in 12 *The Times*, L.R., p. 21. A misfeasance summons having been taken out by the Official Receiver in the winding-up of the above-named company against the directors and Auditors, the Auditors applied for a stay of proceedings as against them on the ground that they were not officers of the company within Section 10 of the Companies (Winding-up) Act 1890. The articles of the above-named company with reference to the audit of the accounts were in substance in the same terms as the audit clauses of Table A to the Companies Act 1862, which, it will be remembered, any limited company other than a banking company is at liberty either to adopt or reject. In the recent case of *In re The London and General Bank, Lim.* (11 *The Times* L.R. 374) it was decided by the Court of Appeal that an Auditor of a banking company regulated by the Companies Act 1879, which made it compulsory on every banking company within the Act to appoint an Auditor, was an officer of the company within the meaning of Section 10 of the Act of 1890. The articles of the London and General Bank contained clauses relating to the audit of accounts, which substantially embodied the provisions of the Act of 1879, and which did not materially differ from the articles of the present company except that the articles of the present company nowhere in terms referred to the Auditors as officers of the company. Mr. Justice Vaughan Williams held that the Auditors were officers of the company within the meaning of Section 10 of the Act of 1890. The Auditors appealed.

Mr. Swinfen Eady, Q.C., and Mr. Eve, Q.C., in support of the appeal, contended that the ordinary professional relationship between a professional man and a company did not constitute him an officer of the company within the meaning of the misfeasance section of the Act

of 1890. That section was confined to persons carrying on the business of the company and having the control of the assets. The word "misfeasance" in the Act of 1890 referred to an act in the nature of a breach of trust, and was not applicable to the responsibility of an Auditor who had been guilty of negligence in the audit of the accounts. It had been held that neither a banker nor a broker nor a solicitor was an officer of the company. There was no obligation on a company, other than a banking company, to employ an Auditor at all, and an Auditor was not a person in the continuous employment of the company, but was appointed annually to perform a single duty.

Mr. Cozens-Hardy, Q.C., and Mr. W. D. Rawlins, for the Official Receiver, contended that this case was not distinguishable from the case of *In re The London and General Bank, Lim.*

Mr. Eve, Q.C., replied.

JUDGMENT.

Lord Herschell: In this case an application is made under the 10th Section of the Companies (Winding-up) Act 1890 to proceed against the directors and the Auditors of the company on the ground that they have been guilty respectively of misfeasance within the meaning of that section. We have not here to determine whether they have been guilty of such misfeasance. We have not the facts before us. We have not even to determine whether the allegations of the summons show a *prima facie* case of what would be misfeasance under the statute. All that we have to determine is whether the Auditors in the present case are persons in a position and coming within the meaning of the word "officers" under the 10th Section, so as to entitle the liquidator to proceed against them. Now, a question very similar to this came before the Court of Appeal in the case of *In re The London and General Bank*. The question there was whether the Auditors of the London and General Bank were officers within the meaning of the section in question. This Court held that they were, and I can see no substantial distinction between that case and the present. I will allude in a moment to the distinctions which have been suggested, but it seems to me that it would be frittering away the case altogether if we were to rest our determination upon any of the distinctions which alone can be made in the present case. Now, I desire to express no opinion upon the question whether *In re The London and General Bank* was rightly or wrongly decided. It may be that the reasoning in that case is open to criticism. It may be that some considerations which bear upon the question were not referred to, or had not full effect given to them; on all that I express no opinion at all. I desire to retain absolute liberty of action, in case it should hereafter become necessary on the question whether

In re The London and General Bank was rightly decided. Now let us see what *In re The London and General Bank* did decide. It decided that the Auditors appointed in that case were officers within the meaning of the section. On what grounds? Under the Act of 1879 certain articles contained in Table A to the Act of 1862, which prior to that Act companies might either adopt or reject as they pleased, became by statute absolutely binding on banking companies. That, even if not strictly accurate, is sufficiently accurate for the purpose of this case. They had to appoint Auditors, and certain provisions were made applicable to them, which were in substance the provisions of Table A so far as Auditors are concerned. Now, the London and General Bank, besides these, what I may call compulsory articles, had also articles of its own. The reasoning in that case was rested largely, I may say mainly, on this—that the Auditors were by the provisions of the Act of 1879, which were made applicable to the bank, made officers of the company. The language of those provisions was dwelt upon as showing that they were officers of the company. It is true, and here comes the distinction suggested, that in that case they were so denominated in an indemnity clause, whereas in the present case they are not so denominated. But it would be far too narrow a distinction to rest any difference of decision on that ground. Therefore, in the present case the articles are in substance the same, the Auditors are created officers, if they are officers in that case, in precisely the same way as in the present case. I can see no substantial distinction between the two. If misfeasance of officers extended to the Auditors in the case of the London and General Bank, it seems to me that no substantial reason can be given why misfeasance of officers should not extend to Auditors in the present case. I cannot in substance distinguish the two cases. But, of course, all that we decide is that, in a case identical with *In re The London and General Bank*, as I take this to be in substance, the Auditor is an officer. We decide that as bound by the previous decision of the Court of Appeal. Beyond that our decision does not go. I say this in consequence of some general observations made by the learned Judge in the Court below, as to which I express no opinion. For these reasons I think that this appeal must be dismissed.

A. L. Smith, L.J., and Rigby, L.J., concurred.

(*Times*, 23 November 1895.)

The case of THE KINGSTON COTTON MILL COMPANY, LIM.

(Decided before Lords Justices LINDLEY, LOPES, and KAY, in the Court of Appeal, on May 19 1896.)

Held that in the absence of suspicious circumstances an Auditor is not guilty of Negligence who relies upon the statements made by trusted Officers of that Company.

This was an appeal by Messrs. Benjamin Pickering and Arthur Edgar Peasegood, the former Auditors of the company, now in liquidation, against an order of Mr. Justice Vaughan Williams under Section 10 of the Companies (Winding-up) Act 1890, making them liable to make good to the assets of the company moneys of the company improperly applied in payment of dividends on the faith of certain Balance Sheets certified by them. The facts in the case were fully reported in Vol. XII., *Accountant Law Reports*, p. 225.

Mr. Haldane, Q.C., Mr. Swinfen Eady, Q.C., and Mr. T. A. Watson were for the Auditors; Mr. Cozens-Hardy, Q.C., Mr. Rawlins, Q.C., and Mr. Marshall Hall were for the Official Receiver and liquidator.

The appeal was argued on May 6, 7, and 8.

Their Lordships now delivered judgment, allowing the appeal.

Lord Justice Lindley said:—This is an appeal from an order made by Mr. Justice Vaughan Williams under Section 10 of the Companies (Winding up) Act 1890, on Mr. Pickering and Mr. Peasegood, the Auditors of the company, ordering them to pay to the liquidator certain sums of money, being the amounts of dividends improperly declared and paid out of the assets of the company on the faith of certain Balance Sheets prepared and signed by the Auditors. The appeal is based upon two grounds—(1) that the Auditors have not failed to discharge their duty to the company and are under no liability to make good the money misapplied; (2) that, even if they have, the proper remedy is by action and not by the summary process to which the liquidator has had recourse. It will be convenient to dispose of the second point first. It has already been decided that the Auditors of this company are “officers” within the meaning of Section 10 of the Companies (Winding-up) Act 1890 (see 1896, 1 Ch. 6; *The Times Law Reports*, Vol. XII., p. 60). The object of that section is the same as that of Section 165 of the Companies Act 1862, which it has replaced. That object was to facilitate the recovery by the liquidator of assets of a company improperly dealt with by its promoters, directors, or other officers. The section applies to breaches of trust and misfeasances by such persons. I agree that the section does not apply to all cases in which actions by the company will lie for the recovery of damages

against the persons named; it is easy to imagine cases of breach of contract, trespasses, negligences, or other wrongs to which the section is inapplicable, and some such have been the subject of judicial decision; but I am not aware of any authority to the effect that the section does not apply to the case of an officer who has committed a breach of his duty to the company, the direct consequence of which has been a misapplication of its assets, for which he could be made responsible by an action at law or in equity. Such a breach of duty, if established, is a "misfeasance" within the meaning of the section, or, to adopt the language used in *Cavendish-Bentinck v. Fenn* (12 A.C. 652), such a breach of duty is a misfeasance in the nature of a breach of trust. This view of the section was adopted by this Court in *In re The London and General Bank* (1895, 2 Ch. 166, 673; *The Times Law Reports*, Vol. XI., pp. 374, 573), and is, in my opinion, correct. On this preliminary point, therefore, which, however, does not touch the merits of the case, the appellants are not entitled to succeed. I come now to the real question in this controversy, and that is, whether the appellants have been guilty of any breach of duty to the company. To decide this question it is necessary to consider (1) What their duty was; (2) How they performed it, and in what respects (if any) they failed to perform it. The duty of an Auditor generally was very carefully considered by this Court in *In re The London and General Bank* (1895, 2 Ch. 673), and I cannot usefully add anything to what will be found on pages 682-84. It was there pointed out that an Auditor's duty is to examine the books, ascertain that they are right, and to prepare a Balance Sheet showing the true financial position of the company at the time to which the Balance Sheet refers. But it was also pointed out that an Auditor is not an insurer, and that in the discharge of his duty he is only bound to exercise a reasonable amount of care and skill. It was further pointed out that what in any particular case is a reasonable amount of care and skill depends on the circumstances of that case; that if there is nothing which ought to excite suspicion, less care may properly be considered reasonable than could be so considered if suspicion was or ought to have been aroused. These are the general principles which have to be applied to cases of this description. I protest, however, against the notion that an Auditor is bound to be suspicious, as distinguished from being reasonably careful. To substitute the one expression for the other may easily lead to serious error. I pass now to consider the complaint made against the Auditors in this particular case. The complaint is that they failed to detect certain frauds. There is no charge of dishonesty on the part of the Auditors. They did not certify or pass anything which they did not honestly believe to be true. It is said, however, that they were culpably careless. The circumstances are as follows: For several years

frauds were committed by the manager, who, in order to bolster up the company and make it appear flourishing when it was the reverse, deliberately exaggerated both the quantities and values of the cotton and yarn in the company's mills. He did this at the ends of the years 1890, 1891, 1892, and 1893. There was no book or account (except the Stock Journal, to which I will refer presently) showing the quantity or value of the cotton or yarn in the mill at any one time. It would not be easy to keep such a book. Nor is it wanted for ordinary purposes. There is considerable waste (20 or 25 per cent. on the average) in the manufacture of yarn from cotton, and the market prices of both cotton and yarn are subject to great fluctuations. The Balance Sheets of each year contained on the asset side entries of the values of the stock-in-trade at the end of the year, and those entries were stated to be "as per manager's certificate." There were also in the Balance Sheets entries on the opposite side of the values of the stock-in-trade at the beginning of the year. The quantities did not appear in either case. The Auditors took the entry of the stock-in-trade at the beginning of the year from the last preceding Balance Sheet, and they took the values of the stock-in-trade at the end of the year from the Stock Journal. The book contained a series of accounts under various heads purporting to show the quantities and values of the company's stock-in-trade at the end of each year, and a summary of all the accounts showing the total value of such stock-in-trade. The summary was signed by the manager, and the value as shown by it was adopted by the Auditors and was inserted as an asset in the Balance Sheet, but "as per manager's certificate." The summary always corresponded with the accounts summarised, and the Auditors ascertained that this was the case. But they did not examine further into the accuracy of the accounts summarised. The Auditors did not profess to guarantee the correctness of this item. They assumed no responsibility for it. They took the item from the manager, and the entry in the Balance Sheet showed that they did so. I confess I cannot see that their omission to check his returns was a breach of their duty to the company. It is no part of an Auditor's duty to take stock. No one contends that it is. He must rely on other people for details of the stock-in-trade in hand. In the case of a cotton mill he must rely on some skilled person for the materials necessary to enable him to enter the stock-in-trade at its proper value in the Balance Sheet. In this case the Auditors relied on the manager. He was a man of high character and of unquestioned competence. He was trusted by everyone who knew him. The learned Judge has held that the directors are not to be blamed for trusting him. The Auditors had no suspicion that he was not to be trusted to give accurate information as to the stock-in-trade in hand, and they trusted him accordingly in

that matter. But it is said they ought not to have done so, and for this reason. The Stock Journal showed the quantities—that is, the weight in pounds—of the cotton and yarn at the end of each year. Other books showed the quantities of cotton bought during the year and the quantities of yarn sold during the year. If these books had been compared by the Auditors they would have found that the quantity of cotton and yarn in hand at the end of the year ought to be much less than the quantity shown in the Stock Journal, and so much less that the value of the cotton and yarn entered in the Stock Journal could not be right, or, at all events, was so abnormally large as to excite suspicion and demand further inquiry. This is the view taken by the learned Judge. But, although it is no doubt true that such a process might have been gone through, and that, if gone through, the fraud would have been discovered, can it be truly said that the Auditors were wanting in reasonable care in not thinking it necessary to test the managing director's returns? I cannot bring myself to think they were, nor do I think that any jury of business men would take a different view. It is not sufficient to say that the frauds must have been detected if the entries in the books had been put together in a way which never occurred to anyone before suspicion was aroused. The question is whether, no suspicion of anything wrong being entertained, there was a want of reasonable care on the part of the Auditors in relying on the returns made by a competent and trusted expert relating to matters on which information from such a person was essential. I cannot think there was. The manager had no apparent conflict between his interest and his duty. His position was not similar to that of a cashier who has to account for the cash which he receives, and whose own account of his receipts and payments could not reasonably be taken by an Auditor without further inquiry. The Auditor's duty is not so onerous as the learned Judge has held it to be. The order appealed from must be discharged with costs.

Lopes, L.J., in the course of his judgment, made the following observations upon the duties of Auditors:—It is the duty of an Auditor to bring to bear on the work he has to perform that skill, care, and caution which a reasonably competent, careful, and cautious Auditor would use. What is reasonable skill, care, and caution must depend on the particular circumstances of each case. An Auditor is not bound to be a detective, or, as was said, to approach his work with suspicion or with a foregone conclusion that there is something wrong. He is a watch-dog, but not a bloodhound. He is justified in believing tried servants of the company in whom confidence is placed by the company. He is entitled to assume that they are honest and to rely upon their representations, provided he takes reasonable care. If there is

anything calculated to excite suspicion he should probe it to the bottom, but in the absence of anything of that kind, he is only bound to be reasonably cautious and careful. His Lordship then referred to the circumstances which led to the Auditors being deceived, and came to the conclusion that they were not wanting in skill, care, or caution, in accepting the figures of the manager, and he concluded as follows:—The duties of Auditors must not be rendered too onerous. Their work is responsible and laborious, and the remuneration moderate. I should be sorry to see the liability of Auditors extended any further than in *In re The London and General Bank*. Indeed, I only assented to that decision on account of the inconsistency of the statement made to the directors with the Balance Sheet certified by the Auditors and presented to the shareholders. This satisfied my mind that the Auditors deliberately concealed that from the shareholders which they had communicated to the directors. It would be difficult to say this was not a breach of duty. Auditors must not be made liable for not tracking out ingenious and carefully-laid schemes of fraud, when there is nothing to arouse their suspicion and when those frauds are perpetrated by tried servants of the company and are undetected for years by the directors. So to hold would make the position of an Auditor intolerable.

Kay, L.J., concurred.

(*Acct. L.R.*, 1896, p. 77.)

The case of THE WESTERN COUNTIES STEAM BAKERIES
AND MILLING COMPANY, LIM.

(Decided before LINDLEY, SMITH, and RIGBY, L.JJ., in the Court of
Appeal, on March 11 1897.)

Held that an Accountant who certifies the Accounts of a Company as Auditor, but who has never been properly appointed as Auditor, is not an Officer of that Company

This was an appeal from a decision of Mr. Justice Stirling. The appellants, Messrs. Parsons & Robjnt, had been employed by the directors to prepare a Balance Sheet and audit accounts of the above company for the year 1889; one of their clerks did the actual work, and signed the name of the firm at the foot of the accounts, vouching for their accuracy. The liquidator, in the winding-up, sought to make the

two partners in the firm liable in respect of dividends declared on the faith of these accounts, by summary process, under the misfeasances clause (Section 10) of the Companies Act 1890. Mr. Justice Stirling held that Messrs. Parsons & Robjnt was an "officer" of the company within the meaning of that section, and was liable. Mr. Parsons appealed.

Their Lordships allowed the appeal with costs.

JUDGMENT.

Lindley, L.J., read the following judgment:—The question raised by this appeal is whether Messrs. Parsons & Robjnt are liable to be proceeded against under that section as an "officer" of the company. To answer this question it is necessary to ascertain who Messrs. Parsons & Robjnt are, and what they have done. They were accountants employed by one of the directors to audit the accounts of the company and to prepare a Balance Sheet for the year 1889, to be laid before the shareholders of the company at their annual general meeting. This they did; he and his partner signed, *per pro.*, a certificate at the bottom, worded, "We have carefully examined the accounts of the Western Counties Steam Bakeries and Milling Company, and find the same to be in accordance with the above Balance Sheet, which shows the correct financial position of the company." The accounts were, in fact, examined, and the Balance Sheet prepared by a clerk of the firm, and he signed the name of the firm at the bottom of the certificate; but no reliance was placed by the appellants upon this circumstance. They admitted their clerk's authority to act for them, and they admitted their own liability for what their clerk did. Messrs. Parsons & Robjnt were paid £12 12s. for their services by a cheque of the company. Now, if Section 10 of the Winding-up Act 1890 contained the word "Auditor," it might well be that Messrs. Parsons & Robjnt, having acted as they did, could not be heard to say that they were not Auditors, and Section 10 might well apply to them. But the word "Auditor" is not in the section, and what has to be determined is whether Messrs. Parsons & Robjnt are officers of the company, or have so acted that they cannot be heard to say that they were not. If all persons who did Auditor's work for a company were officers of the company the case would be easy; but no decision has yet gone this length. An Auditor may or may not be an officer of a company. So may anybody else—*e.g.*, a banker or solicitor. *Primâ facie* such persons are not officers. To be an officer there must be an office, and an office imports a recognised position with rights and duties annexed to it, and it would be an abuse of words to call a person an officer who fills no position either *de jure*

or *de facto*, but who happens to do some of the work which he would have to do if he were an officer in the proper sense of the word. Messrs. Parsons & Robjert performed the duties which an Auditor would have had to perform; it appears to me that they were no more *de facto* than *de jure* an officer of the company. They were simply accountants, called in by the directors to do a piece of work, and they never were, and never pretended to be, or acted as if they were, anything else. In my opinion the decisions in the cases of *The London and General Bank* and *The Kingston Cotton Mills Company* decided two points only—viz., first that Auditors might be officers within Section 10, a proposition which, in the first case, was very stoutly disputed; and, secondly, that the Auditors in those cases were officers of the companies then in question; that is, that the persons there had within Section 10 really filled the office of Auditor in those cases respectively.

Smith, L.J.: If the appellants were officers of the company upon January 30 1890, when they certified the correctness of the company's Balance Sheet for the year 1889, they may be proceeded against by means of such summons, otherwise they cannot be. It has been held by this Court in the case of *In re Kingston Cotton Mills Company* (1896, 1 Ch.D. 6), following the case also in this Court of *In re London and General Bank* (1895, 2 Ch.D. 166), that where a company having articles of association similar to those in the present case, has appointed a person to the office of Auditor of the company, such person is an "officer" within the meaning of Section 10 of the Companies (Winding-up) Act of 1890. It having thus been held that a person appointed by the company to the office of Auditor of the company is an officer within the meaning of the section, we are now asked to take a step further and to hold that a person who has never been appointed to the office of Auditor or to any other office in the company at all is nevertheless an officer of the company if he has performed work which an Auditor if he had been appointed by the company to the office of Auditor would have undertaken and performed. The first case which is relied upon is that of *Gibson v. Barton* (L.R. 10 Q.B. 329), where it was held that a man who performed the work of manager of a company became thereby the *de facto* manager. The learned Judges held that "manager" in the 1862 Act meant manager *de facto*, and that a person who performed manager's work becomes thereby manager; but how does this establish that a person who performs Auditor's work becomes an officer of the company? I agree that performing the work of an Auditor shows the person to be a *de facto* though he may not be a *de jure* Auditor, but to succeed, the liquidator must show that the person is a *de facto* "officer." Some Auditors are officers of a company

and some are not. Those who are officers are within the section, not those who are not officers. It is no good showing that a person performs Auditor's work; it must be shown that he is a *de facto* officer of the company. The next case is that of *Coventry and Dixon's* case (14 Ch.D. 660). There, two directors did the work of directors without being qualified to be directors. Sir George Jessel held them to be *de facto* directors though they were not *de jure* directors, and as such were liable to be proceeded against summarily by way of a misfeasance summons. When this case was under appeal (it was reversed upon another point) Lord Justice Bramwell said if he (that is, the director) has done anything wrong as a *de facto* director no doubt he can be got at under the clause. In this I agree, and if Messrs. Parsons & Robjert had done anything wrong as *de facto* officers they could be got at; but they have done nothing of the sort, for the simple reason they have never become officers of the company at all. I agree that doing the work of a director may make a person a *de facto* director, and the section enacts that a director may be proceeded against by summons. Doing the work of a manager may make a person a *de facto* manager, and the section enacts that a manager may be proceeded against by summons. So in the case of a liquidator. Doing the work of an Auditor may make a person a *de facto* Auditor, but the section does not make an Auditor liable to be proceeded against; it is only when he is *de facto* or *de jure* an officer of the company that he can be proceeded against by summons under Section 10. In this case Messrs. Parsons & Robjert were neither *de facto* nor *de jure* officers of the company; then how can they be said with truth to be officers of the company? All that this Court has heretofore held is that an Auditor may be proceeded against by summons if he is *de facto* an officer of the company. It has not held that a man may be proceeded against by summons when he is neither *de facto* nor *de jure* an officer of the company. The question is not, were the applicants *de facto* Auditors? It is, were they *de facto* officers?

Rigby, L.J., concurred.

(*Times*, 12 March 1897.)

The case of CITIZENS' AUDITOR v. THE CITY COUNCIL,
MANCHESTER CORPORATION.

(Decided before CAVE and LAWRENCE, J.J., in the Queen's Bench Division, on March 18 1897).

Held that Burgesses are entitled to inspection of Minutes of Town Council and Committees.

The action brought by Mr. Norbury Williams, one of the citizens' Auditors, and Mr. Edward Woodall against the Manchester Corporation, to determine the extent of the right given by Section 233 of the Municipal Corporations Act to a burgess of a borough to inspect the minutes of the Council and its Committees, came on for hearing in the Queen's Bench Division on March 18. Cave and Lawrence, JJ., sat as a Divisional Court to try special cases. Mr. C. A. Russell, Q.C. (instructed by Messrs. Hinde, Milne & Bury, Manchester), appeared for the plaintiffs, and the Corporation were represented by Mr. Asquith, Q.C., M.P., and Mr. M'Morran, Q.C. (instructed by the Town Clerk, Mr. W. H. Talbot). Amongst the gentlemen present in Court were Mr. Norbury Williams, Mr. Talbot, Aldermen Gibson and Higginbottom (chairman and deputy-chairman of the Gas Committee), and Mr. Charles Nickson (superintendent of the Gas Department of the Corporation).

In the statement of the case it was set forth that: The plaintiffs are citizens of the city of Manchester, which has a population of upwards of 529,000, and of which the number of enrolled citizens is 87,627. The defendants are a municipal corporation regulated by the Municipal Corporations Act 1882, which provides as follows by Section 233:—"The minutes of proceedings of the Council shall be open to the inspection of a burgess on the payment of a fee of one shilling, and a burgess may make a copy thereof or take an extract therefrom. A burgess may make a copy of, or take an extract from, an order of the Council for the payment of money." Certain standing orders for the management of the business of the Council were made by the Manchester Council. Among them were the following:—"X. (1) No motion or amendment shall be made or proposed or any discussion allowed upon the confirmation of the proceedings of the several Committees with reference to any matter within the province of a Committee which does not appear upon the minutes to be confirmed; but any member may put a question to the chairman of the Committee with reference to any such matter." "XI. (1) An epitome of minutes of the several Committees of the Council shall be prepared each month under the direction of the town clerk and be submitted to the chairman of each Committee prior to its being sent to the Council." The Council have appointed no fewer than twenty-one Committees, and the ordinary business of the Corporation

is regulated and managed by them. The minutes kept by the Council merely refer to the proceedings of the Committees by stating that the proceedings of each Committee have been approved. Minutes of the proceedings of Committees are also recorded in books, which are submitted for the approval of the Council. The acts or proceedings of the Committee which are approved by the Council are not specifically recorded in the minutes of the Council, but are approved by reference to the minutes of the several Committees, and can be ascertained only by inspection of such minutes. The plaintiffs made an application for an inspection of the minutes of the proceedings of the Gas and Rivers Committees, which are referred to in the minutes of the Council as having been read and approved during the past two years, and they tendered the fees mentioned in the section. They were not allowed to see them, but were referred to the Council minutes. The Corporation objected to produce the Minute Books so kept by the Gas Committee and Rivers Committee respectively, on the ground that the production of the minutes of the Committees would be inimical to the interests of the citizens of Manchester. The Corporation, having regard to the foregoing considerations, were of opinion that it was not consistent with the public interests to permit inspection of the minutes of the Committee in all cases; and, as they were advised that such inspection could not be claimed as a right under the statute, they declined to permit the inspection claimed by the plaintiffs. On the part of the plaintiffs it is alleged that when the proceedings of any of the Committees have been approved by the Council, and such approval has been recorded, as in the specimen minutes, they are entitled to inspect the minutes of such Committee for the purpose of ascertaining what acts or proceedings of such Committee the Council have approved.

Mr. Russell, on behalf of the plaintiffs, said the question which had arisen in the present case was a peculiar one. The minutes of the Town Council of Manchester were, as the plaintiffs alleged, kept in such a form that it was quite impossible to ascertain what the proceedings actually were. The point to be determined, therefore, was whether the way in which the Corporation had kept the minutes of the Council was such that the plaintiffs were entitled, for the purposes of ascertaining what the proceedings were, to refer to the minutes of the Committees. The minutes of the Council certainly did not give the details of the work done. For instance, the minutes of the Corporation would read, "The proceedings of the Watch Committee having been read, resolved that the same be approved." This rendered it necessary that one should go to the minutes of the Committee referred to in the minutes of the Council and search them to enable one to ascertain what it was the Council had approved. The plaintiffs, therefore, said

they were entitled, on the payment of a shilling, not only to see the minutes of the Council, but to see the minutes of the Committees. Counsel admitted that the Manchester Corporation had adopted a form of minute which most skilfully concealed the details of the work done. Thus, if a sum were recommended by the Parks Committee for building a band-stand, the fact of such sum being allowed ought to appear, which it did not on the minutes as now settled. There was no record of order of payment of money. Section 233 was thus rendered nugatory.

Mr. Asquith, for the Corporation, said he appeared for that body to say that they contested this matter in no contentious spirit, but merely to get guidance from the Court as to what was their duty in the matter of the keeping of these minutes. There had been some suggestion of deliberate concealment.

Mr. Russell: Oh no.

Cave, J., said it was clear that the Council under the Act should let the burgesses know all the acts of the Corporation.

Mr. Asquith said the Corporation had been keeping their minutes in the present form for 60 years, and they had always been willing to allow the burgesses to inspect the Committees' minutes when it was consistent with the public interest. In some cases it would be most inexpedient to allow the burgesses to see all the preliminary details.

Cave, J.: I think the burgesses are entitled to ask to be shown what has been approved by the Council.

Mr. Asquith: The Corporation, as I understand, are willing to concede that, but what they object to in the public interest is the looking at the Minute Books of Committees which contain preliminary proceedings leading up to the final act.

Cave, J.: There I should agree with you. I do not think they are entitled to do that. But the difficulty is, can you suggest a way in which what they are entitled to see can be reconciled with what they are not entitled to see?

Mr. Asquith: Perhaps a practical solution of the difficulty may be arrived at if the document described as an "epitome," which is submitted to the members of the Council immediately before they meet, and which I am instructed contains a summary of the decisions actually arrived at by the Committees, were treated as part of the minutes of the Council, and allowed to be inspected. But the prayer of this claim is that they may inspect the minutes of proceedings of any Committee.

Cave, J.: That is going rather far, but the difficulty is to see how they should be separated, because the Corporation make the minutes part of the proceedings.

Mr. Russell: All we ask is the right to see the minutes for the purpose of ascertaining what acts and proceedings of such Committee have been approved. If the epitome shows us the acts, that will do.

Mr. Asquith: So long as it is made clear that the Corporation are not bound to disclose any confidential preliminary matters to which I referred, they will have no objection.

Cave, J.: I do not see that they are bound to disclose such confidential matters.

Mr. Russell: I admit that I do not see anywhere in the Act of Parliament a right to inspect minutes of Committees as such. I do not think that is what is contended for here. I was referring to the minutes of the Committee so far as they were reported to the Council.

Cave, J.: The epitome will answer your purposes. Mr. Asquith does not object to your seeing that, and I think that will do.

Mr. Russell: The Council are, of course, the masters of the form in which they keep their minutes. As long as they keep them in the present form I cannot ask for any more.

Mr. Asquith: I feel, and the town clerk quite agrees with me, that the form in which the minutes have been traditionally kept does give considerable colour to my friend's claim. I repeat that the Council are willing that the acts of the Committee approved shall be inspected by the burgesses, but not the Minute Books.

Mr. Russell: We have only had the epitome offered to us now. It has been expressly refused down to the present. All we want is a declaration from the Council that the burgesses are entitled to inspect the acts of the Committees approved by the Council.

Mr. Asquith: The acts of every Committee approved by the Council are to be open to inspection.

Mr. Russell: I must ask for all acts submitted for approval, because some acts of the Committee may not be approved.

Mr. Asquith: Yes; I agree that the acts of every Committee submitted for approval are to be open to inspection in the future.

It was agreed that the declaration should be that the burgesses are entitled to inspect the minutes of acts of the Committees submitted to the Council for approval, and an order was made accordingly. After consultation between counsel it was agreed that the plaintiff's costs in the action should be borne by the Corporation.

(Manchester City News, 19 March 1897.)

The case of WILDE AND OTHERS v. CAPE AND DALGLEISH.

(Decided before the LORD CHIEF JUSTICE and a Special Jury, in the Queen's Bench Division, on May 27 1897.)

Held that an Auditor is liable for Losses occasioned by his not fulfilling his Contract.

In this action the plaintiffs, Messrs. Wilde, Burchell & Burchell, a firm of solicitors, claimed damages from the defendant, Mr. Dalglish, who carries on business as an accountant at 8 Old Jewry, E.C., under the name of Cape & Dalglish, for negligence and breach of duty in auditing the plaintiffs' books and in preparing and certifying their Balance Sheets.

It appeared that the defendant had been employed to audit the plaintiffs' books for the years ending September 30 1890 to 1895, and to examine and certify Balance Sheets for each of those years. The negligence complained of was that the defendant did not carefully examine the plaintiffs' Pass Books and omitted to discover certain fraudulent entries made in them. By these fraudulent entries the plaintiffs' cashier had defrauded them of £1,756 4s. 9d., which sum they now claimed from the defendant. The defendant's case was that all he was bound to do under the terms of his employment was to see that the plaintiffs' books were brought to a correct balance and to raise a Balance Sheet and Profit and Loss Account as between the partners, taking the entries and balances appearing in the books as correct. He denied that he was employed to make a cash audit, or check receipts or payments, or examine the Cash Book or Bank Book in any way, or to be in any way responsible for the accuracy of the cash transactions. These, the defendant contended, were the conditions of employment arranged with Mr. Cape, the defendant's deceased partner, by the plaintiffs in 1883. In 1884 Mr. Dalglish entered into partnership with Mr. Cape, who died in 1889, and since that date he had audited the plaintiffs' books with the object above stated—*i.e.*, to ascertain the Profit and Loss Account as between the partners, accepting the accuracy of the entries appearing in the books. He repudiated all responsibility for not having discovered the defalcations of the plaintiffs' cashier.

After evidence had been given by the plaintiffs, during the midday adjournment the parties came to terms.

Mr. Bigham said that his client was unaware of the terms which had been arranged between the plaintiffs and Mr. Cape, and did not know that he was to check the accounts in the Pass Book. After hearing the

plaintiffs' evidence as to the arrangements made with Mr. Cape, Mr. Dalgleish thought that, with regard to the loss caused by the defalcations of the cashier, he ought to meet the plaintiffs half-way, and was prepared to consent to judgment for them for £850.

JUDGMENT.

The Lord Chief Justice gave judgment for the plaintiffs for this amount, and added that it was only fair to Mr. Dalgleish to say that the settlement of the case must not be taken as any reflection on his personal skill or care. The difficulty had arisen solely owing to a misunderstanding on his part as to the terms of his employment by the plaintiffs.

(*Times*, 28 May 1897.)

The case of MARTIN *v.* ISITT.

(Decided before Lord Chief Justice RUSSELL and a Special Jury, in the Queen's Bench Division, on 3rd and 4th March 1898.)

Monthly Audit—Action against Auditors for alleged Negligence—Defence that the Proper Materials were not supplied to do the Work—Judgment by Consent.

This was an action brought by Messrs. James Martin & Sons, milk and grain merchants, against Messrs. Isitt & Co., Chartered Accountants, for negligence in not checking the Cash Book and the Bank Pass Book, whereby a clerk was enabled undiscovered to embezzle £612 19s. 2d., the property of the plaintiffs. The defendants alleged that they were unable to properly proceed with their agreed work owing to the neglect of the plaintiffs to give proper facilities, and in particular they complained that the books were not properly posted up and were full of errors, of which the defendants were unable to get the necessary explanations.

Mr. E. Tindal Atkinson, Q.C., and Mr. Haigh were for the plaintiffs; Mr. Carson, Q.C., and Mr. T. M. Stevens for the defendants.

It appeared that in 1887 Mr. Eldrid, now a member of the defendants' firm, agreed with plaintiffs to do certain work which was not material to the present action, and also undertook the "monthly checking of all your books" for an inclusive fee of thirty guineas, afterwards increased to sixty guineas. It was not the defendants' duty to audit, but merely to "check" the books. To enable this to be done clerks were sent down to the plaintiffs' head office at Brockley, and they spent there a very considerable number of hours doing the requisite work. The books

were written up and posted by the plaintiffs themselves; with this the defendants had nothing to do. It further appeared that a man named May, in charge of a branch of the plaintiffs' business, received money, and in a weekly statement sent to the plaintiffs credited himself with payments into a bank, which payments should in ordinary course appear in the London and County Bank Pass Book of the plaintiffs. In fact, from the last week of November 1896 until the end of March 1897 he habitually embezzled the money. The plaintiffs would enter in their Cash Book the amount alleged by May to have been paid into the bank; the Pass Book, of course, would not agree with the Cash Book, and the plaintiffs complained that this was not discovered until the first days of April 1897. It was admitted that the discovery was made by, and was due to the work of, the defendants; but it was then alleged against the defendants that the discovery should have been made earlier. The reply of the defendants to this was that the state of the books was such, and the queried items—the explanations of which were constantly delayed—were so numerous, that they were unable to proceed fast enough to keep pace; and that, in December 1896, they were still engaged in dealing with the entries relating to the summer months of 1896. Further, they said that they were requested by the plaintiffs not to proceed with the work in January and that the month of February was wasted away to the default of the plaintiffs. The senior member of the plaintiffs' firm was called, and gave evidence supporting his own and negating the defendants' case, but his cross-examination was not concluded when the Court rose for the day.

Before resuming the hearing the next morning, a consultation took place between counsel, and as a result, Mr. Carson stated that he understood that it would not now be contended that the defendants had been negligent or unskilful in the way in which they had done their work, but that the plaintiffs would rest their case on a breach of one term of the contract—viz., the agreement to attend monthly. That being so, and recognising that the plaintiffs had suffered a loss, the defendants were quite willing to share that loss to a certain extent, and consequently terms had been arranged.

The Lord Chief Justice said that as he understood the case as placed before him, no allegation of negligence or unskilfulness was now made, but that it was urged that the defendants should have attended somewhat earlier than they actually did; that was a question to be tried, but he thought the action of the parties in arranging the matter to be very proper.

The case of COX *v.* EDINBURGH AND DISTRICT TRAMWAYS
COMPANY, LIM.

(Decided before Lord KYLLACHY, in the Outer House of the Court of
Session, on June 16 1898.)

*Held that when a Tramway Company alters its system from Horse Traction to
Cable Traction nothing need be written off Capital Account before paying
Dividends out of Current Profits.*

Lord Kyllachy gave judgment in the suspension and interdict at the instance of Robert Cox of Gorgie, M.P., residing at 34 Drumsheugh Gardens, Edinburgh, against the Edinburgh and District Tramways Company, Lim., 1 South Charlotte Street, Edinburgh. The complainer seeks to have the respondents interdicted from declaring or paying any dividend on any shares of the company out of the capital of the company; from paying any dividend except out of the net profits of the whole business of the company; and from declaring any dividend until due provision has been made out of the net revenue for loss of capital or depreciation of assets on Capital Account; and, in particular, until the sum of £20,000 or other loss arising on the realisation of the existing stock of horses, cars, and plant has been provided for.

Lord Kyllachy said: This is an action brought by a shareholder of the Edinburgh Tramways Company by which he seeks to restrain the respondents from paying a certain dividend for the first half of the current year 1898; or at least from paying that dividend until provision is made for a certain loss, which, it is stated, has arisen, or is about to arise, upon the realisation of the existing stock of horses and cars belonging to the company. The respondents dispute the relevancy of the complainer's statement, and the parties (without renouncing probation) are agreed in asking a judgment on relevancy. They are also agreed that for that purpose a certain minute of admissions shall be taken as forming part of the complainer's statement. The facts upon which the complaint is rested are, shortly, these. The respondents—a limited company—hold (in substance) a lease for a term of years of the Edinburgh tramways. They pay a rent to the Corporation for the heritable subjects, and their business consists in working the tramways, for which purposes they provide the necessary rolling-stock,* including a number of cars and horses. It has lately been arranged that, in consideration of an increased rent, the Corporation shall convert the tramway lines into what is known as cable tramways, and the existing stabling into a station or stations, for the fixed machinery required for working the cables. This conversion, it is said, although not yet completed, will be

so in the course of the present year; and, of course, the result will be to supersede the use of horses for haulage, and also, to a large extent, to supersede the existing cars by cars of a different construction. What the complainer alleges is that, upon the sale which must follow of the horses and cars at present in use, there will be a loss to the company of over £20,000—that is to say, a difference of that amount between the prices realised and the cost or value of the horses and cars as at present standing in the company's books. He also alleges that the cost to the company of providing new cars and "grippers" will be about £45,000, and that in addition there will be the cost of cables for the entire system. He does not allege or suggest that the conversion in progress is not and will not be beneficial to the company, or that the directors of the company have not fully considered its effect on their financial position, or that anything has been, or is being, done which will leave the company with assets insufficient to pay its debts. His case simply is that the transaction involves an element of a certain sacrifice of existing assets. That is, as I read it, and as I think it must be read, the meaning and substance of his averments, and in particular his statement that "It is believed and averred that there will be a loss or depreciation upon the assets of the company in respect of such realisation, amounting to not less than £20,000." I do not go into the question as to an additional alleged loss on temporary stabling; or as to the sufficiency or insufficiency of certain sums paid out of revenue into Suspense Accounts, to meet that and other alleged losses. For the purposes of the argument it seems enough to take the alleged prospective loss in the realisation of the horses and cars. That is sufficient to raise the complainer's case. For I must at least at this stage assume, what the complainer states, that the sum at the credit of the Suspense Account is quite inadequate to meet the alleged loss or deficiency on the horses and cars. Now I have had a full and very able and interesting argument on a general question which has of late years occupied, it is said, the attention of the English Courts—the question, namely, whether and how far loss or depreciation of assets forming the capital stock of a limited company bars the payment of dividend until that loss or depreciation has been recouped. It was, on the one hand, contended that the principles as applied and expounded by the English Court of Appeal in the cases of *Lee v. Neuchâtel Asphalte Company* (41 Ch.D. p. 1) and *Verner v. General Investment Company* (2 Ch. (1894) p. 239) are conclusive against the complainer—establishing, as it is said these cases do, that with respect to fixed or permanent, as distinguished from circulating or floating, capital, there is no rule of law by which such capital must be maintained at its original or any particular value; but that, on the contrary, so long as there is a

surplus, sufficient for dividend, of annual revenue over annual outgoings—that is to say, a surplus arising on a Revenue Account properly kept—the state of the company's Capital Account is, as affecting dividend, a matter of no moment. On the other hand, it was argued for the complainer that the decisions referred to have not yet been considered by the House of Lords; that they are contrary to previous decisions, and are not well-founded in principle. It was further argued that, even assuming the law to be as there held with respect to fixed capital or assets, the horses and cars here in question are not properly assets of that character. They are, it is said, subject to continuous waste, and to waste requiring to be replaced, and that such waste (or, rather, the cost of its replacement), however large and however caused, must always and necessarily form a charge against revenue. Now, I may not perhaps be bound by these English decisions, although, of course, they are decisions of high authority; but I may say at once that I have no difficulty in accepting not only their results, but their general doctrine. At the same time, I do not myself see that the respondents in this case require to appeal to those decisions or to the principles new or old there expounded. Nor, on the other hand, am I quite clear that if the respondents' defence did require such an appeal, such appeal (I mean as an appeal to those particular authorities) would be entirely conclusive. The view I take of the present case is shortly this. It is not at all, in my opinion, a case such as might have presented itself if, for example (the respondents still working the tramways by horse traction), a fire or other catastrophe had occurred by which, say, their horses perished, and their cars were destroyed. In that case there would, of course, have been beyond question a loss of assets in the most real sense, and a loss beyond doubt requiring to be replaced. And that being so, questions, I think, of some difficulty would or might have occurred as to how far the necessary replacement could properly or justifiably be charged to capital. It does not, however, appear to me that (taking the facts of this case as they appear on the complainer's statement and the minute of admissions) we have here to deal with anything which can be considered as in any real sense a loss or depreciation actual or prospective, of the respondents' assets. The selling off of their horses and cars is, or will be, a voluntary act on the part of the company. It is part of a scheme or transaction on which the company has embarked presumably for the benefit and not for the detriment of their undertaking, and if such scheme or transaction involves, by reason of enforced sale or otherwise, a sacrifice in one direction, such sacrifice will at least presumably be compensated by a corresponding gain in some other direction. I am, I think, entitled to hold that that is the view of the directors and of the company. I

am also, I think, entitled to hold that they entertain that view on reasonable grounds—grounds, at all events, which are not impeached by the complainer. But if that is so, it is surely a strong suggestion that I should assume without inquiry that the company, as a going concern, will suffer upon the total transaction a loss equal to the loss on its discarded assets, or, on the other hand, that I should allow a proof as to the effect on the company's general assets of the proposed conversion from horse to cable traction. I am certainly not prepared to make such an assumption, nor, on the other hand, am I prepared to allow such a proof except upon averments of a quite different kind from those with which I have here to deal. In saying so I do not proceed on any law or doctrine established or said to be established by recent decisions. I proceed on a principle as old as the beginning of company law—the principle, namely, that in matters of the kind here in question—matters necessarily of estimate and opinion—a company is presumably the best judge of its own affairs. In such matters the Court will not readily interfere with the company's action, and it will not do so at all except on averments which involve practically a case of fraud or dishonesty. The truth is that the complainer's argument involved, as it seemed to me, the assumption that capital sunk—that is to say, capital not represented by tangible and available assets—is in all cases to be considered as capital lost. Of course, if that were so, the question or kind of question would here arise which arose in the two English cases of which we have heard so much; but such a proposition has never, so far as I know, been, as yet at least, advanced. The case suggested by Lord Justice Lindley, of expenditure made in starting a newspaper, is a very good illustration of the impracticability of such a doctrine. But, apart from extreme cases, few things are, I should think, more common in ordinary business than operations of the kind with which we are here concerned. A merchant or manufacturer desires to enlarge his premises, satisfied that it will pay him to do so. He accordingly pulls down old buildings which have a certain value, and he replaces them by others at perhaps great cost. There is thus, of course, in a sense, the sacrifice of a permanent asset, and it may quite well happen that the new buildings if put into the market would not fetch a sum equal to the value of the old building plus the cost of the new. But for the purposes of the trader's business the result may be entirely the other way, and the presumption is that the trader is satisfied that it is so. If he is so satisfied he will certainly not consider that he has sustained a loss of capital, or feel bound to carry the cost of the old building to the debit of his Profit and Loss Account for the year. Similarly, a manufacturer requires or resolves to discard certain machinery and to replace it with other machinery more effective or more economical. Here, again, the

sacrifice in the case of the old machinery is simply an item in the cost of the change. So, also, when a railway company, as sometimes happens, alters its gauge, or substitutes, say, steel for iron rails. The operation necessarily involves a sacrifice of old material. But the assumption always is that the operation as a whole enhances the value of the concern or undertaking. And although it may be a prudent and proper thing to provide for the recurrence of such expenditure, and to set up a renewal fund, that is a question which the trader considers for himself, and one as to which, even in the case of limited companies, Courts of law are not accustomed to interfere. On the whole matter I am of opinion that the complainer has stated no relevant case for interfering with the proposed dividend, or for granting him interdict in terms of any part of his prayer.

His Lordship accordingly refused the note, with expenses.

(*Glasgow Herald*, 17 June 1898.)

The case of REGINA v. WILLIAMS.

(Decided before Lord RUSSELL, L.C.J., BRUCE, KENNEDY, RIDLEY, and DARLING, JJ., in the Queen's Bench Division, on 23rd January 1899.)

Falsification of Accounts.

This was a case stated for the consideration of the Court for Crown Cases Reserved from the quarter sessions for Cornwall.

The prisoner was convicted of falsifying accounts. He was collector of poor rates for the parish of Perranuthnoe, and had entered in the overseers' accounts with the parish a "balance in hand £131 10s. 5d.," though that money was not forthcoming. The facts sufficiently appear from the judgment, in which the conviction was upheld.

JUDGMENT.

The Lord Chief Justice said in this case the prisoner was indicted under 38 and 39 Vict., c. 24, section 1, for falsifying accounts. The facts were that on April 10 1890, the prisoner was appointed collector of poor rates for the parish of Perranuthnoe, in Cornwall, and he remained in that post. It appeared that there were two sets of accounts kept, one of which was referred to in the seventh and eighth counts of the indictment. This would appear to have been an account between the prisoner and the overseers; but no evidence had been offered at the trial on those charges. There was a second account which the prisoner kept for the overseers of the state of accounts between them and the parish. It was in respect of that account that the charges were made. That

account was one which showed on the debit side the moneys received from the poor rates and the balance, if any, from the last account, and on the credit side the moneys paid away by the overseers, as, for instance, to the treasurer of the union, or the parish council, or for salaries, &c. That being so, what was said to be the falsification? It was this—that the prisoner, with intent to defraud, made an entry thus, “balance in hand £131 10s. 5d.” Was that entry true or false? So far as could be seen that was perfectly true, for it stated that £131 10s. 5d. was due from the overseers in respect of that account. If the balance had been stated in any other way it would have been erroneous. But it was stated that it must be taken to mean that the prisoner had that sum in his pocket, whereas he had in reality spent it. It certainly did not mean anything of the kind. If it had been his own account with the overseers different considerations would have applied; but, looked at as an account between the parish and the overseers, it was literally and exactly true, and the Auditors had found it correct. It was quite true that the defendant had told one of the overseers a lie, for in answer to a question on the subject he had said that the money was all right when it was really gone, and it might be that the prisoner could have been convicted of embezzlement; but there was no evidence of falsification of accounts, and the appeal must be allowed.

The other learned Judges concurred.

(*Times*, 23 January 1899.)

The case of THOMAS *v.* THE CORPORATION OF DEVONPORT.

(Decided before the LORD CHIEF JUSTICE (LORD RUSSELL), A. L. SMITH, and VAUGHAN WILLIAMS, L.JJ., in the Court of Appeal, on 2nd November 1899.)

Held that an Elective Auditor cannot claim Remuneration out of the Borough Fund, but is entitled to reasonable Remuneration as Auditor of Urban Sanitary Authority.

In this case the plaintiff is the Elective Auditor of the defendant corporation, and is also designated by statute as the Auditor of the urban sanitary authority. He claimed remuneration as Elective Auditor out of the borough fund, and he also claimed remuneration for twenty-three and a-half days' work as urban sanitary Auditor during a number of years past at the rate of two guineas a day. Phillimore, J., who tried the action, held that the plaintiff was not entitled to any remuneration as Elective Auditor, and with regard to his work

as the Auditor of the urban sanitary authority said the plaintiff was barred by the Statute of Limitations with respect to some of the days claimed for, and he had taken longer than was necessary to do the work in the later period for which he claimed. The learned Judge held that £34 paid into Court by the defendants in respect of sixteen days' work during the past two years was sufficient remuneration for the plaintiff's services as Auditor of the urban sanitary authority, and therefore gave judgment for the defendant corporation on both issues. Hence the plaintiff's appeal.

JUDGMENT.

The Lord Chief Justice, in giving judgment, said this was one of those cases under the statute in which the corporation was also the urban sanitary authority. The case really would have been unarguable on the part of the plaintiff if it had not been for some observations made by Phillimore, J., in delivering judgment. As regarded the claim in respect of auditing the corporation accounts as such it was quite clear that there was not a shadow of ground for saying that the plaintiff as Elective Auditor had any claim at all. The receipts of the corporation as such were brought into and formed part of the borough fund, and payments of all accounts legally made by the corporation must be paid out of that borough fund. Parliament had in clear and distinct terms laid down the appropriations which might be made out of the borough fund in the statute regulating the matter. If the plaintiff had been a servant of the corporation there was ample power given to the corporation to pay him out of the borough fund in respect of any services which he rendered. But he was not a servant of the corporation. He was elected by the burgesses of the borough under a statute giving the burgesses power to elect an Auditor. There was no claim in respect of such services. As regarded his services as Auditor of the urban sanitary authority, he was entitled to be compensated at a rate of not less than two guineas for every day on which he was properly employed on the work. If the matter had simply rested there, there would have been an end of it, and it would not have been possible for this Court to have reviewed the judgment of the learned Judge of the Court below, because he found as a fact that four days in each half-year—or eight legal days in each year—was ample for the work which the plaintiff did. Unfortunately, as he (the Lord Chief Justice) thought, Phillimore, J., had used some language which suggested too narrow a judgment of what the proper duties of the Auditor of the urban sanitary authority were. He (the Lord Chief Justice) did not subscribe to the doctrine that the Auditor's sole duty was to see whether there were vouchers, formal and regular,

justifying each of the items in respect of which the authority sought to get credit upon the accounts. That was an incomplete and imperfect view of the duties of such an Auditor. Such an Auditor was not only entitled, but justified and bound, to go further than that. He should make a fair and reasonable examination of the accounts, and see whether there might not be, amongst the payments made, payments which were not authorised or which were illegally made, and if he so discovered such payments it would be his duty certainly to make them public, certainly to report them to the authority itself, and certainly to report them to the burgesses, who had created that authority. But granting all that, he (the Lord Chief Justice) saw no reason for believing that eight days would not be adequate in which to do the work, and he saw no reason for disturbing the judgment of the Court below.

Smith and Vaughan Williams, L.JJ., said they entirely concurred, and the appeal was accordingly dismissed with costs.

(*Times*, 3 November 1899.)

The case of MOXHAM AND OTHERS v. GRANT.

(Decided before A. L. SMITH, COLLINS, and VAUGHAN WILLIAMS, L.JJ., in the Court of Appeal, on the 15th November 1899.)

Held that Shareholders of a Company who have received Dividends out of Capital with a knowledge of the fact, must refund to the Directors.

This was an appeal from the judgment of the Divisional Court (Lawrance and Channell, JJ.), reported in 15 *The Times* L.R. 180; (1899) 1 Q.B. 480. The plaintiffs were directors of a company named Cory's Steamers, Lim. The company owned a steamship named the *Primrose*, which was lost in 1894. The underwriters paid £719 2s. 6d. in respect of the loss. That sum represented capital, as it represented the steamship. In April 1894 the directors sent a circular to the shareholders in the following form:—"We have a sum of money in hand from insurance received on account of the loss of the *Primrose*. We propose remitting 10s. per share. If you see no objection, we will send you £—, being 10s. on your — shares, on your sending a receipt on enclosed form, and provided all the shareholders consent. There will be a considerable sum more to receive for insurance of *Primrose*." The form of receipt was as follows:—"Received of Cory's Steamers, Lim., the sum of £—, being a reduction of 10s. per share on the — shares held by me." In reply to the circular the defendant sent the following letter:—"I quite agree with the proposition of your

letter of April 10, and enclose my receipt for £13, being 10s. on my 26 shares." Other similar payments were made to the defendant, the total amount being £35 15s. Upon December 29 1896 a winding-up order was made against the company, and on December 22 1897 the liquidator of the company obtained an order under Section 10 of the Companies (Winding-up) Act 1890, declaring that the payment to the defendant and other shareholders of the various sums, amounting in the whole to £719 2s. 6d., was a payment of part of the capital of the company and was unlawfully and improperly paid in reduction of the capital of the company, and it was further ordered that the directors should pay to the official liquidator the sum of £719 2s. 6d. The order was expressly made without prejudice to the right of the directors to be recouped by the shareholders the amounts paid by the directors to them. The directors, the plaintiffs, then brought an action against the defendant to recover the £35 15s. they had paid to him. The County Court Judge gave judgment for the plaintiffs, and the Divisional Court affirmed the decision. The defendant appealed.

JUDGMENT.

The Court dismissed the appeal.

Smith, L.J., said that it was admitted that the £719 2s. 6d., which was paid by the underwriters on the loss of the *Primrose*, was part of the capital of the company. The directors and shareholders agreed that they did not want this money as capital and resolved to divide it. Therefore the shareholders knew that it was part of the capital of the company. It was not a case where shareholders received money of the company in ignorance that they had no right to receive it. There was no order of the Court obtained for the reduction of the capital of the company. When the company was wound up the liquidator discovered what had been done, and, in his Lordship's opinion, the liquidator might have taken proceedings against everyone who had received portions of the £719 2s. 6d. Instead of doing that, the liquidator, as the most convenient course, took proceedings against the directors who had received the money and who had distributed it among the shareholders, and he recovered the whole amount from them. The directors thereupon brought an action against the defendant to recover from him the amount which he had received, and which the directors had been compelled to pay to the liquidator. What was the position of a shareholder who had received money of the company with notice that it formed part of the company's capital? It seemed to his Lordship that the position of the shareholder in such a case was, as laid down by Sir George Jessel in *Russell v. Wakefield Waterworks Company* (L.R. 20 Eq. 474,

at p. 479), that of a constructive trustee. That being so, the rule of equity as between two trustees had been explained in many cases, and in *Chillingworth v. Chambers* (1896, 1 Ch. 685) the matter was fully discussed by Lindley and Kay, L.JJ., and himself, and he would only refer to one passage in his own judgment (at p. 707):—"As between two trustees who are *in pari delicto*, the one who has made good a loss occasioned by a breach of trust for which the two are jointly and severally liable may obtain contribution to that loss from the other." The case cited in support of the proposition was *Lingard v. Bromley* (1 V. and B. 114) (see p. 710 of the report). In the present case the defendant took his portion of the £719 2s. 6d. with notice that it formed part of the capital of the company. He became a constructive trustee, and must recoup his co-trustees, who had been compelled to pay it back, the amount so received by him. Upon that ground the judgment of the Divisional Court was right. His Lordship also thought that the doctrine laid down in *Bonner v. Tottenham Building Society* (1899, 1 Q.B. 161) applied. He desired to add that the passage in "*Lindley on Companies*" 5th ed., pp. 389, 390) did not apply where the shareholders took the money with notice, as here, nor where one person had been compelled by process of law to pay in relief of another.

Collins, L.J., concurred. When the circumstances of the case were understood, it was clear that the liquidator could have enforced against each shareholder repayment of the moneys received by each. That he could enforce repayment against the directors to whom the whole fund had originally passed lay at the root of the matter. Therefore they began the discussion with these facts. The directors, being the persons who had collected and distributed the fund, were liable to repay it to the liquidator, and the persons to whom it was distributed were also liable to the liquidator, and the directors were compelled to pay the whole sum distributed. Further, that payment had necessarily gone in relief of the shareholders. Upon those facts—namely, a payment by compulsion by one of a sum for which another was liable to the same person—there arose by implication of law a right in the person paying to be recouped by the person relieved. Having got those facts, which entitled a person so paying to indemnity or contribution, what was the answer attempted to be set up? The only possible answer was that these persons were joint tortfeasors, and that there was no right of indemnity or contribution. Lord Denham, in *Belts v. Gibbins* (2 A. and E. 57, at p. 74), in dealing with *Merryweather v. Nixon* (8 T.R. 186), said that that case "seems to me to have been strained beyond what the decision will bear. The present case is an exception to the general rule. The general rule is that between wrongdoers there is neither

indemnity nor contribution: the exception is where the act is not clearly illegal in itself." He (the Lord Justice) did not suppose that any of those who dealt with this money thought that there was any illegality in doing what was done. The only illegality was a technical one; it was an *ultra vires* act. It had been held over and over again that money paid in breach of trust to persons who took it knowing the payment to be a breach of trust did not constitute those persons joint tortfeasors. Channell, J., dealt with that point and with the line of authorities relating to it; and Vice-Chancellor Bacon, in *Flitcroft's* case (21 Ch.D. 519, at p. 527), also so held. That disposed of the case. But he (the Lord Justice) would deal with the argument whether or not there was a trust. The only bearing this had lay in establishing that the person who received the money received it in such circumstances as made it capable of being recovered back. If the money was paid to the shareholder unearmarked, so that the liquidator could not claim it as money had and received to his use, the chain of consecution out of which the right to indemnity arose was broken. Unless the payment was made in relief of the person against whom the indemnity was claimed, the claim for indemnity was gone. Therefore, it must be shown that the liquidator would be entitled to sue the shareholder. That was established if the liquidator could follow the money, and that was so in the present case, because the shareholder received it with notice, from which, if he knew his law, he must have known that the directors had no right to pay it to him. The whole claim, therefore, was established. The payment by the directors to the liquidator was in relief of an existing liability of the shareholders, and was a payment which they were compelled to make. Therefore there arose upon common law principles a right of indemnity. There was also the same right on the general rules of equity, and this right was not affected by any question of the parties being joint tortfeasors.

Vaughan Williams, L.J., delivered judgment to the same effect.

(*Times*, 16 November 1899.)

The case of REGINA v. DEXTER, LAIDLER, AND COATES
(*Re* DEXTER, LAIDLER & CO., LIM.).

(Decided before Mr. Justice GRANTHAM and a Jury, at the Durham Assizes on 30th November 1899.)

Prosecution for Fraud of an Accountant and others concerned in the formation of a Company.

Jesse Dexter, commercial traveller, of Glasgow, formerly of Jarrow; William Laidler, clerk; and George Henry Coates, accountant, New-

castle, were indicted for having conspired together to issue a false prospectus of Dexter, Laidler & Company with intent to defraud the public.

Mr. Joel, in opening the case, said that prior to 1895 the father of Dexter carried on a small timber business at Jarrow. About June 1895 the elder Dexter died, and the defendant Dexter took over the business. Immediately before that the elder Dexter had made an arrangement with his creditors, so that the business was not at that time in a flourishing condition. Dexter put into the business £100 he had borrowed, £200 he raised on a reversionary interest, and another £800 he borrowed from his mother. With this capital Dexter started in 1895. He obtained a lease of the wood-yard and buildings for a term of 80 years at £150 rent a year. In April 1897 Laidler, one of the defendants, was taken into partnership, and the firm became Dexter, Laidler & Co. Between April, when the partnership began, and July 1898, when the company was floated, a period of fifteen months, the net loss on the business, after deducting trade expenses, was £981. The turnover of the business in 1895 was £3,364, in 1897 £4,904, and in the half of 1898 £2,353. Early in 1898 a Mr. Duffy had advanced £1,000 on timber held by the firm at Tyne Dock, so that the business was then in difficulties, and this same timber was afterwards handed over to a Mr. Roper under an authentic document for £500. In 1898 the firm started a business in Newcastle under the title of the Empire Furnishing Company, of which Mr. Ions became the manager. The ascertained turnover of that business was £600 a month, with a total of £1,800 in the three and a half months up to the flotation of the company. During the 15 months since the beginning of the partnership the total turnover at both Jarrow and Newcastle was £8,730, and the ascertained loss on the trading was £1,732, the realised loss on a sale being very much more. These figures showed that the business was in difficulties. Early in 1898 Dexter and Laidler called in the defendant Coates, who was a Chartered Accountant, and on June 30 the whole business was registered as a company, under the title of Dexter, Laidler & Co., Lim. Prospectuses were prepared, and 10,000 were issued broadcast on July 6. The capital of the company was fixed at £25,000 in £1 shares. The vendors agreed to take 7,500 of the shares in part payment of the £12,500 at which the business had been valued, and sold to the proposed company, and a dividend of 10 per cent. on the subscribed and paid-up capital was guaranteed for three years. Counsel, reading from the prospectus, said it was stated that the business at Jarrow had been carried on at a profit for some considerable time, as was shown by the report of the accountant. The Newcastle branch had

been entirely successful, and had yielded a handsome profit. The directors expressed the belief that with additional capital the business might be largely extended, and to show their confidence in the undertaking they had agreed to take 7,500 fully paid-up shares as part payment of the purchase-money. In the prospectus there was a report by George C. Coates, Chartered Accountant, of Post Office Chambers, Newcastle, stating that he "had investigated the accounts of the business for the three years ending 31st ult., and he had to report that the sales had increased from £8,000 in 1895 to over £15,000 during the past twelve months." The report concluded with the expression of a belief that with the increase of capital the profits of the company would be doubled. The prospectus contained a further certificate from a firm of valuers of a valuation of the mills, offices, plant, machinery, timber, and stock at Jarrow, and furniture, &c., at Newcastle. These properties were valued at £11,404 1s. 9d., which would have been a fair figure if the properties had really belonged to the firm. As regards the mills and yard at Jarrow, that was simply leasehold, and belonged to the landlord, while the lease itself was mortgaged. Part of the timber, too, referred to in the prospectus as belonging to the firm was mortgaged to other people. These statements were misleading, and constituted the false representations for which the defendants had been indicted. Proceeding, Mr. Joel pointed out that three days after the company was registered Dexter and Ions applied to Mr. Pybus, solicitor, Newcastle, who was acting as solicitor to the company, for a loan of money. Mr. Pybus was informed, however, that there had been an execution put in against the Jarrow mill, and this aroused his suspicions. The money was not lent, and as he felt satisfied that he was assisting to float a company that was in difficulties, he felt it to be his bounden duty to put an end to it. He went to the bankers and found that some £500 worth of shares had been applied for. He insisted that all deposits should be returned to the intending subscribers, and the public therefore lost nothing over the matter. Subsequently the firm was made bankrupt, and afterwards the present proceedings were instituted against the defendants. Evidence was then called.

William Devonport Wild, from the office of the Registrar of the Newcastle Bankruptcy Court, put in a file of the examination of Dexter and Laidler on their own petition. The trustee, Mr. Bowden, was appointed on the 23rd August 1898.

William Mark Pybus, Junr., of Pybus & Son, solicitors, of Port Chambers, Newcastle, said he had exclusive charge of this matter during the flotation of this company. Witness explained the process of making entries in the Minute Books in respect to all interviews held.

The first transaction the firm had with the defendants was when Dexter and Laidler called and asked if he could get a client for a cargo of timber, and upon a valuation of Mr. Dixon witness recommended Mr. William Roper to lend £400. On the afternoon of the same day, June 1, Coates and Ions being present, witness was asked if his firm would act as solicitors to a proposed company, Dexter, Laidler & Co. They talked about it being an old-established business, and so on, and of course witness knew it by name, and he said they would, subject to having a valuation and accountant's report. They agreed to that, and witness suggested that Messrs. Bowden & Sons, who generally acted for Messrs. Pybus, should be asked to make a report, but Coates suggested that as he had audited the books for several years he should act, and this was agreed to. The defendants told him among other things that the capital was to be £25,000, that their annual profits were over £1,000 a year, that Mr. Ions would be the promoter of the company, but would receive nothing as promoter, that they would guarantee a dividend of 10 per cent. for three years from the 1st July, and discharge all liabilities. They told him that Dexter and Laidler would be directors. Ions undertook to furnish a prospectus, and he afterwards did produce one, which was put in before the magistrates as the original document. The principles of the prospectus were never altered. He was told that the book debts were about £1,500 and the profits £1,000 a year. On the 6th June he saw Ions, who gave him instructions to prepare the agreement, so that he would act as trustee to transfer the assets to the company. On the 7th June he saw Dexter and Laidler as to the agreement, and on the 8th a general agreement was entered into. On the 9th he received a letter from Ions, with a copy of Coates' report written in type on note paper of the Empire Furnishing Company. Next day he had an interview with the defendant Coates about the document, but at a later interview Coates said he wished to make a slight alteration in his report; he stated that he wished to say in his report that in his opinion the increased capital to be obtained would more than double the past profits. Coates asked him what he thought about that, and witness said he did not think it of very much value, as it was only a matter of opinion and a matter of figures. At a subsequent interview witness told Coates that the report must be an honest and a fair one, and he said that as it stood now, with the addition, it fairly represented what the profits of the business had been. On the 15th June he saw Ions and Dexter, and with them discussed the memorandum and articles of association, and on the 20th June he sent a copy of the final report to Ions. On the 25th June he saw Ions, who told him the directors were being seen, and he would let him know who they were to be. On the 27th June witness saw Ions

and Laidler, who informed him that Duffy, Dalzell, and themselves would be directors, and at that interview he pointed out that the report was not a strong one at all, and had far better show the profits of the business year by year. They refused to alter it, and he believed their reason was they did not want to disclose too much of their business. On the same day he wrote to Ions to go through the memorandum, and on the 20th he saw Laidler, Dexter, Ions, Coates, Mrs. Coates, and Dalzell. All signed but Ions, and his firm signed, and on the 30th June the agreement was sent up to be registered. Witness told Coates afterwards that the book debts were stated to be £1,500, but he did not see it in the report, and asked him to amend it, but witness never received it, and the report remained without it. On the 4th July he saw Ions, Coates, and Mr. Hedley, and they discussed whether the book debts should go into the valuation of Hedley and Turnbull, or the report of Coates, and the former thought it should go into the latter's report. On the 5th July he saw Ions, Dexter, and Coates, with whom he went thoroughly over the prospectus. He read it to them word for word, and they said it was right. Ten thousand copies were printed on the 5th July. On the 6th July he saw Dexter and Ions, who discussed the question of Dexter's management, and on the 9th July Dexter, Laidler, and Ions came and saw witness's father in his presence. They stated they had a bill of £800 falling due that day, but were disappointed, and were unable to pay their wages, and asked witness's father to lend them £40. His father refused, and said that was not his business. Dexter fainted, and witness's father, feeling sorry for him, said he could have it on giving him his personal assurance of repayment. Just at that moment the cashier knocked at the door and called him out, and told witness he had just been up at Court issuing a writ, and saw just by accident that there was an execution out against Dexter and Laidler. They said they were temporarily pressed for money, but the business was a very flourishing one, and they were making profits as was said in the prospectus. Witness told them it was very wrong not to tell him, and they said they had another solicitor acting for them in that. He made inquiries that day, and found there were executions and other matters, as the result of which he told them he was going to the bank to insist upon the return of the deposits. He found that about 500 shares had been taken up. Witness did have the deposits returned to all the applicants. On the 13th July he saw Mr. Ions, and told him what he had done; he pointed out that it was very wrong trying to foist a company of this kind on the public, when he knew the statements in the prospectus were incorrect. He had an interview on the 13th with Dexter. Witness's father was then present, and Dexter asked if it were not possible to sell out their own shares and raise

money on debentures, and he said they would have nothing to do with the matter unless they put their affairs entirely into the hands of his firm. On the 18th July a petition was filed. It was not his duty as solicitor to investigate the assets of a company; the firm must be company promoters to do that. The firm were not informed of any mortgage on the lease. Dexter said he had the lease at home. Witness accepted the report, and his answer was the same, so far as all the actual business was concerned. In cross-examination, witness said that Coates did say to him that as he had had the accounts through his hands he should make the investigation of the accounts of the business with Mr. Bowden.

Walter Mark Pybus, Senr., of the firm of Pybus & Pybus, solicitors, Newcastle, gave evidence as to Dexter and Laidler waiting upon him on the 18th July and requesting him to give him a remittance in order to pay wages, as they had not sufficient. In the course of the interview Dexter became unwell, and after giving him brandy he came round, and the interview was resumed. Witness, feeling sorry for him, was about to call the cashier for the purpose of giving the money which was wanted, upon Dexter's personal security, when the cashier made a communication to him by which he discovered that there were several writs out against Dexter and Laidler. Witness went back and told them what he had heard, and said it was very improper for them not to have disclosed the fact that the writs were out. He told them that one thing was perfectly clear, and that was that in no circumstances must they come to allotment, and told them to call the directors together, and that they should pass a resolution that there should be no allotment, and that the amount paid on the applications should be returned. Dexter and Laidler consented to Mr. Bowden being called in to make an examination of the books, and Coates then suggested that as he was acquainted with the books and accounts he could be of material service, and suggested that he should act in conjunction with Mr. Bowden. Witness said he might give Mr. Bowden any assistance he could, but that he (witness) could not agree to his acting.

Witness, in cross-examination, said the defendants never offered any objection to the suggestion to return the subscribed capital.

John Ralph Hedley, valuer, late Hedley & Turnbull, now Hedley & Anderson, gave evidence of valuation. He said he spent a whole day at East Quarry, Jarrow, with Laidler and Ions valuing buildings, offices, machinery, and plant. He was not told anything about any of the timber being the property of J. G. Laidler, or gentlemen named

Roper or Duffy. His valuation was for £6,044 6s. 3d. He valued all the machinery, and also valued the building, but was not told that the lease on the latter had been mortgaged.

Joseph William Turnbull, who valued the whole of what was alleged to belong to the company, fixed the valuation at £9,500, which included timber at Tyne Dock, which Ions took him to see. He was not told there was a charge on that.

William Roper, corn importer, said Ions tried to borrow money, stating that the business was extending so rapidly that they had not sufficient capital to keep pace with the extensive trade which was being done, and proposed converting the business into a limited company. On the strength of this, witness paid £400, and got warrants for timber lying at Tyne Dock. He lent another £100 on some timber which was put in at the Northumberland Docks. Witness sold the timber for £552, and he returned the surplus to the trustee.

William Middleton, solicitor, said he heard Mr. Duffy swear that he had bought the timber outright. Mr. Duffy said he had lent £1,000 on some timber.

Thomas George Bowden, Chartered Accountant, Newcastle, and trustee in bankruptcy of Dexter and Laidler's affairs, said the whole sales from March 1898 to July 1898 were £6,950. During the partnership the total for Newcastle and Jarrow businesses was just over £8,000 for 15 months before the formation of the company. It was impossible for any man to investigate the accounts of a business, and to have come to the conclusion that the business should increase from £8,000 to over £15,000 during the past 12 months. The £1,482 book debts in the statement of affairs had realised up to the present £800 or £1,000.

Cross-examined: Asked whether £150 was not something more like a fee for the accountants' work than £50, witness said it depended upon the nature of the work. He had heard that Coates had undertaken to take 100 shares and £50 in cash for examination of the books.

For the defence, Mr. Shortt, at the outset, asked his Lordship to rule whether Coates was an official of the company who could thus be brought under the Act.

His Lordship ruled that, inasmuch as the company had been registered, and his name appeared on the prospectus, he was.

George Henry Coates said he was called in as a Chartered Accountant in this matter, being approached by Mr. Ions. He saw

some of the books afterwards, principally the Sales Books. He also saw the Delivery Notes and Press Invoice Book. He got otherwise verbal information. He also saw the books of the Empire Furnishing Company, and made out the sales from it, but he had nothing to do with the formation of the company. There was an agreement for services generally that he was to receive £150, of which £100 was to be in cash and £50 in shares. He made the remark that he was willing to receive £50 in cash and £100 in shares, and he received £50 in cash.

Asked by his Lordship as to the meaning of the term "general services," witness said he supposed it was meant that he was to get shareholders. The report in the prospectus was not as his original report put it. The last sentence with reference to the book debts and that the sales were at the rate of £15,000 a year were not in. He did not write his original report on the Empire Furnishing Company's paper, but on his own, and it was sent to Mr. Pybus through Ions.

Cross-examined by Mr. Joel: Witness said his report contained the words "at the rate of" before the figures £15,000. He had not seen the type-written report until it was produced at the Police Court. Witness added that his point was a simple one, and that was that the report in the prospectus was not his.

Cross-examined: Witness said that if the words "at the rate of £15,000 a year" had appeared as he intended them it would be quite true in regard to the last year.

Canon Moore Ede, rector of Gateshead, was called as witness as to the character of Laidler. He had known Laidler and his family for eighteen years, and knew him to bear a very good character throughout the town generally. He might express his own opinion in words he used towards him, "I quite understand him being a fool, but I don't believe he has been a knave."

The Judge: It's not evidence. (Laughter.)

Mr. Carrick also gave him a good character.

Mr. Joel, in summing up for the prosecution, pointed out that Ions was also indicted, but he had run away, and it was not surprising that for the defence it should be put forward that he was the arch conspirator against these three innocent men. It was perfectly true men might deceive themselves as to their business when forming a company, and if that were so no man ought to be charged with the crime of merely exaggerating and putting a fanciful view on their business. But what the Crown said in this case was that this was not a case of that kind. They suggested that there were facts and figures to satisfy

them that there was no justification that out of that business, which had been small and was in the death-grip of impending insolvency and bankruptcy, they should evolve this scheme.

Mr. Shortt, addressing the jury, said he did not intend to defend the issue of the prospectus in its then form. This was a business which had been carried on for 30 years, which under old Mr. Dexter had been a large and flourishing business. They had it that owing to a breaking of building societies that the late Mr. Dexter had been crippled, and was it not in the trend of circumstances that the business should sink to the level they saw it in '96? The figures showed quite plainly that it had increased between 1896 and 1898. This report, acting on instructions and information supplied to him, was prepared in a year when the business had not suffered from this fall. If there had been an attempt to defraud, why would they have gone back to the time when the business was flourishing to compare with the business between '96 and '98? It showed an honest desire. That they were pressed for capital no one would deny, and a large business hampered for want of capital was sure to be in difficulties. To hide their condition they had gone to a high-class firm of solicitors. It was suggested that they did this so that they might use the good name of that firm as a decoy to investors. There was no attempt to deceive Messrs. Pybus, and from the beginning to the end of the prospectus it was clear on the face of it that all that was wanted was capital, and it was thought the best way to raise capital was to float this company. As to the timber, there was £5,000, and only charges to the extent of £500 on it. As to the machinery, it was agreed a Mr. Bentley was entitled to £100 worth, and that as far as they could tell this was the total charge against it, and even in regard to the last referred to machinery, Messrs. Dexter and Laidler had given bills. As to the accounts, it was admitted the books were not kept as they should be. The original report, the only one signed by Coates, was not forwarded to Mr. Pybus—only a copy, type-written on Empire Furnishing Company's paper. Mr. Pybus never had the original, although he had asked Ions to send him a signed report. Only one was signed, which Ions kept, and they had repeatedly asked for its production, but it was not forthcoming. The point was did they deliberately conspire to defraud because they had made a mistake? Was Coates, a Chartered Accountant, going to ruin himself for £50?

Mr. Mellor put the case before the jury as being one of two young men of no experience, men of youth and energy, trying to raise the wreck of a business. Without sufficient capital they get into difficulties. They saw in the future a large business if they could only get the

capital. They saw the business increasing, and they thought there was a way to do it by getting the public to subscribe. This was a bad time to float a business; this was a bad time for people to fail to float a company when so many companies had been floated and failed. This was not one of those cases of some unknown millionaire with a business worth £5,000 floating a company of £100,000, with the right honourable this or that, a few golden guinea pigs, on the directorate. Nor must Coates be made the scapegoat. What did they go to Messrs. Pybus for? They were young men of little experience; they went to the solicitors and paid them fees to keep them right. And at the finish, as soon as these young men knew they had permitted inaccurate statements to go before the public, they sent notice to the bank. Who was defrauded? Counsel laid stress on the absence of Ions, whose prospectus, no doubt, it was from beginning to end. He pointed out by the second clause of the prospectus the promoters agreed to discharge all debts and liabilities up to the date of registration, and therefore until that date Dexter and Laidler had no right to say that there were any charges on the timber. He hoped the jury would not make these young and inexperienced men the catspaw to avenge those gigantic swindles which have disgraced this country.

His Lordship, in summing up, said the jury had heard a good deal about preventing fraudulent companies being put upon the public. An Act of Parliament had been put through the House of Commons, but failed to pass the House of Lords, in regard to company promoting, because some doubt was felt as to who was to be responsible. They would never solve these difficulties until they could make the solicitors liable. There had been no attempt made, so far as he knew, to do it. He did not mean to say or suggest for one moment that Mr. Pybus did anything that was dishonourable, or that he was a party to these frauds, if they were frauds; but what he did say was this, that if a solicitor would put his name on the front of a prospectus as a solicitor to a company, he should be made by Act of Parliament responsible for all the legal powers, all statements made there which he could investigate, and find out whether they were true. Until something of the sort was done his impression was they never would stop these frauds. It was said in a celebrated case, exactly one of these cases, only a much bigger one, by a solicitor, when asked by a Judge what his part of the business was, "For preparing the front page of the prospectus, and that is all; and when I have done that and get something for the public to take up, that is all." What part of the prospectus, he asked—why, the name of a good solicitor. When people saw the name of a good solicitor they thought it was all right. They did not find out, and had.

not been told that the solicitor washed his hands of the matter; they saw his name and assumed it must be all right, and would go in for it. That was the reason the public had been defrauded to the extent they had, because the solicitors did not do what in his judgment they ought to do—find out whether what was stated was true or not. In this case he could not exonerate Messrs. Pybus from their moral responsibility, as solicitors, of not investigating the position of what their subsequently honourable conduct would have stopped in its infancy. It was the duty of a solicitor to protect, and to take care that he did not let his name be used to cover frauds on anybody, whether in the case of company promoters or anybody else. It would have been disastrous to the public if Mr. Pybus had not, as an honourable man, when the time came that he was warned, merely by accident, stopped it. His Lordship also said that the valuation also was not worth the paper it was written on in the circumstances, inasmuch as the buildings and unexpired tenancy, valued at £3,380, were, as an asset, worth £150 less than nothing, owing to a mortgage and liabilities.

The jury found the prisoners guilty, and they were each sentenced to twelve months' hard labour, and ordered to be put in the second-class division.

(*Durham County Advertiser*, 1 December 1899.)

The case of THE IRISH WOOLLEN COMPANY, LIM. v. TYSON
AND OTHERS.

(Decided before the LORD CHANCELLOR, and HOLMES and FITZGIBBON,
L.JJ., in the Irish Court of Appeal, on the 20th January 1900.)

Held that when the Accounts of a Company have been falsified, and Dividends improperly paid out of Capital in consequence, the Auditor is liable if the Falsifications might have been discovered by the exercise of reasonable Care and Skill.

On Friday, in the Court of Appeal, judgment was delivered on the appeal by Mr. Edward Kevans, Chartered Accountant, 22 Dame Street, Dublin (one of the defendants), against the decision given by the Master of the Rolls, reported in 25 *Accountant Law Reports*, p. 89. The question before the Court was simply whether Mr. Kevans was, or was not, responsible for the non-detection of the frauds.

Serjeant Dodd and Mr. C. O'Connor, Q.C. (instructed by Mr. Richard Davoren), appeared for the appellant.

The Right Hon. The MacDermot, Q.C., and Messrs. Wright, Q.C., Blood, Q.C., and W. F. O'Rourke (instructed by Messrs. William Findlater & Co.), appeared for the respondents.

Lord Justice Holmes, in delivering his judgment, referred to the career of the company, which, he said, was formed in June 1887, for the purpose of promoting the woollen industry in Ireland, the original capital being £6,000. For some time at the commencement the business was almost entirely confined to the purchase of woollen goods from Irish manufacturers. In the year 1889 the directors resolved to develop their undertaking by seeking to establish their home trade, and for this purpose they increased their capital. The prospectus announcing this resolution alluded to the success that had attended the operations of the company up to that time, and held out more brilliant prospects for the future. The whole of the additional capital, however, was required to pay off debts previously incurred, and could hardly be used for the purpose of opening up new business. Between the years 1888 to 1895, nine Balance Sheets were presented to the shareholders, each showing considerable net profits; and during all this period dividends were paid which never once fell as low as 5 per cent., amounting to £4,649. There is not the slightest evidence of the soundness of the financial position of the company until its operations were suspended, when Mr. Carnegie—the Auditor's representative, who was examining the accounts—noticed a double entry. The mistake was a trifling one, and he was satisfied with the explanation given by Mr. Crawford, who had been for some time the accountant of the company. Crawford and Johnston abandoned their positions, and the Balance Sheet for the last period (1895) showed a deficiency of £11,107. The company, by order of the Court, was directed to be wound up compulsorily, and Mr. Garde—who was himself formerly in the employment of the defendant Auditor—found that, although the company was just solvent as regards its creditors, its capital had entirely disappeared, and I presume it was his report that led to the bringing of the present action. It appears that Crawford, acting either by himself or with Johnston, the warehouseman, was a defaulter to a very large extent. Mr. Kevans says, in his letters of the 22nd and 24th of January 1896, “that although the whole of the items that made up Crawford's deficiency were apparently received within the three months ending 31st December 1895, it is highly improbable that he could have abstracted all that money in so short a period of time, but that it was impossible to say how far back exactly the defalcations extended.” The defendant was held guilty in connection with Crawford's fraud, and I therefore pass away from this portion of the case, which relates to only a small part of the losses sustained by the company. To account for

the rest it is necessary to go more fully into the way the business was carried on. The directors, who were paid no fees for the first two or three years, were originally selected by lot; and Mr. Peter White was appointed managing director; Mr. Tyson was appointed secretary at £250 per annum; and the rest of the staff—examiner and packer—at £150 and £75 per annum respectively. Mr. Tyson did not long remain secretary, and was succeeded by Mr. McDonough, and subsequently by Crawford. Mr. White, in one of his letters, referred in a somewhat gloomy manner to the large annual amount of money paid to the officers in the shape of salaries, and recommended such a change being made as would reduce the annual expenses to £600. White's recommendation was accepted, and from that date Crawford was appointed secretary. He only received 35s. per week, and his income from the company never seemed to come up to £150 a year. I presume that Johnston did not receive more. Mr. Kevans was the first Auditor of the company, and he provided the books which, in his judgment, were necessary for keeping the accounts. They consisted of:—(1) Cash Book; (2) Customers' Ledger; (3) Creditors' Ledger; (4) Day Book; (5) Invoice Guard Book; (6) Petty Cash Book. It cannot be denied that these were sufficient to show the true financial position of the business of the company, if they had been honestly kept. The MacDermot commented upon the absence of one book, but I attach no importance to this. The multiplication of books, if written up by different parties, may be a check upon fraud, but in this case all the bookkeeping was done by a single officer who, if dishonest, would take care to make the books appear perfectly straight. There was another book, referred to in the evidence, kept for the private use of the directors, but whatever its significance may be it could not affect Mr. Kevans. In February 1891 there occurred a circumstance materially bearing upon the case. After that time the Auditor's fee was increased to £40, the consideration being a "monthly audit." It was not understood by this that a Balance Sheet, or Profit and Loss Account, was to be prepared for each month, or that a monthly statement was to be submitted to the directors. It was a monthly investigation for the purpose of checking fraud or error. It was, as Mr. Kevans himself says, "a system of monthly checking with a view to the half-yearly audit." Mr. Kevans seems to have done little of the actual work himself, and the evidence varies as to the nature of the supervision which he gave to it; the investigation of the books he deputed to his assistants—namely, Mr. Roche, Mr. Garde, and Mr. Carnegie, and it must be on the faith of their representations that he certified the Balance Sheets. I presume this course is not unusual, and that an accountant with a large business is not supposed to do everything himself. The Auditor is bound to give

reasonable care and skill, but this can also be exercised by his deputy. I do not think there is anything to be gained by considering in the abstract the duties of an Auditor of a joint-stock company. He is entitled to see the company's books and the materials for their books, and also to ask for explanations. But he is not called on to seek for knowledge outside the company, or to communicate with customers or creditors. He is not an insurer against fraud or error; and if fraud is alleged it must be shown with precision the acts of negligence for which he is said to be responsible. Nine Balance Sheets were prepared, and the figures on some represent the aggregate amount of many items, but I propose to deal only with matters that have been referred to during the hearing. There are three sets of figures with which I will deal:—(1) Stock-in-trade; (2) sundry debtors; (3) sundry creditors on the liability side of the Balance Sheet. Taking these in order, I find that Mr. Garde, in his evidence, drew a distinction between the home stock and the stock in America, which was never mentioned in this Court. I do not fully understand this, as Mr. Kevans can only be held responsible from the 4th of January 1892, and at that date the American trade had been abandoned. The Master of the Rolls expressed a doubt, with which I agree, as to whether it was the duty of the directors to take stock with their own hands. It was taken by Mr. O'Callaghan, and I agree with the Master of the Rolls that he (Mr. O'Callaghan) did quite as much as he could be expected to do. There was certainly no duty cast on the Auditor to take stock. What he did was to have the calculations checked in his office, and this was done with proper care. Mr. Kevans said he was particularly careful as to the deduction for discount, and, as far as I could gather, the universal rate of 10 per cent. seems reasonable. Moreover, an Auditor has nothing to do with the terms upon which the company, or a trader, buys or sells. As to No. 2, the charge in this is that the allowance made for the trade discount of $2\frac{1}{2}$ per cent. was omitted. This is a purely technical question. Mr. Kevans says that the proper method of dealing with these debts was to return them as they stood in the books, and to bring the discount, when it was allowed, to the Profit and Loss Account. Mr. Pixley said it would not be scientifically correct to deduct these discounts. This seems to be in accordance with common sense, and it is to be noted that although Mr. Garde, as liquidator, corrected the Balance Sheets by marking off these discounts, he never thought of doing so when conducting the audit. As to the provision for the "bad debts," if there is any one thing upon which an Auditor is dependent upon the officers it is the writing off, or the making of a prospective allowance for, bad debts. He has no personal knowledge of the customers, and Mr. Kevans seems to have taken particular

attention in reference to this. (See questions 2,125 to 2,127 in the evidence.) He said "he had some special knowledge on the subject, that he saw all ascertained bad debts duly written off, and that there was a fund amounting to £500 as a provision therefor." For the foregoing reasons there is no ground for alleging negligence against Mr. Kevans on the "assets side" of the Balance Sheet. As far as this portion is concerned, I think the Balance Sheets were properly and carefully prepared, and there was nothing dishonest or negligent on the part of anyone; but if there was, it was not on the part of Mr. Kevans or of his representative. Now, dealing with "sundry creditors"; here evidently there is a fraud, and a curious thing is that no one seemed to have derived any benefit from the fraud. Dealing with the invoices, the learned Judge detailed the practice in connection with the statements of accounts being laid before the meeting, and said, the Ledger was used for the purchases made and for the payments on account thereof. If, then, all this were rightly done it would be easy for the Auditor to ascertain the amounts due to the creditors, but unfortunately the books were not correctly kept. The creditors' accounts in the Ledger did not show all the goods purchased up to the time of the audit, nor could the Auditor discover the omissions on account of many of the invoices being either "suppressed" or not put into the book until at a later date—a process described as "carrying over." There is some doubt as to whether the deficiency arose from the suppression or the carrying over, but my impression is that the whole of it comes within the last-mentioned class, for at the end of 1894 we find they amounted to £4,095. Mr. Peter White is now dead, and he should not be condemned unheard, but it is difficult to believe that this system was not within his own knowledge. As chief promoter he was no doubt anxious to see that the company was successful; Crawford, who was the secretary, appears to have continued the process. It seems strange that a system of fraud so long continued, and for so extensive a period, was never detected by the Auditor. Once or twice he noticed something, and the explanation that was given was "that the goods were not taken into stock." The question is, was it negligent not to have seen this? There is no doubt that both the suppression and carrying over of invoices would have been detected if the Auditor had called for the creditors' statements of accounts upon which payment was ordered, and compared them with the Ledger. I should have thought this was part of the Auditor's duty for many reasons; but all the accountants examined, except Mr. Southworth, stated that this course is never taken unless there is something to arouse suspicion. Mr. Pixley, the eminent London accountant, says it could not well be done except in the case of a very small concern. In the face of such

evidence I should not leave myself at liberty to hold that Mr. Kevans' assistants were guilty of negligence in not looking at these statements of account if they were engaged in an ordinary audit. Little time is allowed for doing so; but in this case there was this system of monthly checking. From the time that Crawford was accountant in 1890 the accounts of the company were completely in his hands. Now, White for the two years following may have given general directions, but he was often away in America for months at a time, and it is clear that the monthly audit was instituted for the purpose of seeing that he (Crawford) would do his work regularly and honestly. I am unable to conceive how, if there was nothing wrong about this monthly checking, it did not lead at an early period to the detection of the frauds in this Ledger. Mr. Kevans ought to have found out, by the accounts, the payments that were made—and no better means could be adopted than that of a comparison with the statements of accounts. It ought to have been done in some way, and, if it had, detection would have been certain. I do not base my decision on this alone; apart altogether from the statements of account and the monthly check, I do not understand how the carrying over of the invoices could have escaped detection by the accountant, who should have used due care and skill and who was not a mere machine. The invoices carried over were ultimately posted to the Ledger. If they were posted to their true dates, it would be at once apparent that they were not entered in at the proper time. If they were posted under false dates, why was this not detected when the Ledger Accounts were checked with the invoices? and when no invoices came into the books, it is admitted that this ought to have excited suspicion. For these reasons I am of opinion that if due care and skill had been exercised, the carrying over and the suppression of invoices would have been discovered, and the Auditor is liable for any damage the company has sustained from the understatement of liabilities in the Balance Sheet due to this cause since January 4 1892. I consider that not only are Mr. Kevans and his assistants not free from blame for this, but also for the mechanical way the audit was carried out. I desire to say that, although I have carefully read the evidence, I have not attempted to examine the books of the company out of Court. I, at one time, thought of doing so, but, on consideration, feared that they might lead me into error. That some damage has been sustained by the company is clear; and it will be observed that I have said nothing about the measure of the damages. Theoretically, damage resulting from negligence has been assessed in money, but it would be premature to consider it now.

Lord Justice Fitzgibbon: I entirely concur with the judgment that Lord Justice Holmes has delivered, and there are a few matters on which I desire to offer some independent observations:—

First.—What is the measure of the defendant Auditor's duty in a case such as this?

Second.—What is the evidence of the particular case of the breach of that duty?

Third.—A few words upon the question of damages.

As regards the measure of the duty of a gentleman employed, as Mr. Kevans was in this case, the result is the same, as it occurs to me, in all cases in which professional skill is employed, except one, the peculiar instance of a barrister. The measure of duty is the bringing of reasonable care and skill to the performance of the business directed to be done, having regard, first to the contract of employment, then to the character of the business itself, to the remuneration of the defendant, and to all the other circumstances of the case. In strict rule, however, the measure of the duty is to be ascertained by applying to all the circumstances of the case the best consideration, so as to ascertain what ought to have been done under the circumstances. Now, in all the three English cases, and also in this case, the Auditor was bound by the articles of association of the company. In one English case it was put forward for the Auditor that he had never seen the articles of association, and it was admitted that he had never read them, but, nevertheless, it was held that if he did not see them, he was at least bound to do all that was required just as if he had seen them. In this case Rules 150 and 157 of the articles of association prescribe the duties of the Auditor, and it is not suggested that Mr. Kevans did not see them. "Once at least in every year the accounts of the company shall be examined, and the correctness of the statement and Balance Sheet ascertained by one or more Auditor or Auditors." Now, it appears that half-yearly statements were submitted to the directors, and I gather that Mr. Kevans discharged his duties half-yearly, but I shall deal with the case entirely on the assumption that he did it only once a year, because his half-yearly examination probably would not be as complete as the one completed at the end of the year. The 157th rule of the articles provides—"That the Auditor shall be supplied with copies of the statements of accounts *seven* days before the intended meeting, and it shall be his duty to examine the same with the accounts and vouchers relating thereto, and to report to the company in general meeting thereon." These are the two rules that define his duty. Rule 158 is, however, important, as showing the materials that were to be placed at his disposal. "The Auditor shall have a list delivered to him

by the directors of all the books kept by the company, and shall have reasonable access to the books and accounts of the company, and may in relation thereto examine the directors, or other officers of the company." Now, there are two specific things that Mr. Kevans was charged with. In the first place, it was practically left to him to say what books the company ought to keep, and therefore he, in the position of a skilled accountant, was really made an adviser as to what the set of books were that he was to examine, and I take it for granted that the books recommended were sufficient. Another matter was, that in the course of the business they had to some extent ascertained by actual experience what was necessary for their protection. They (the directors) made an arrangement with the Auditor that there should be a monthly checking, and therefore he was bound, dealing with the set of books that he himself provided, to check these books once a month and to audit them once a year. Now, I am not going to minimise the distinction between checking and auditing. I do not agree at all with a great deal of what has been presented to us that Mr. Kevans was to have done in the monthly checking, but the monthly checking was a "checking at the time," a preparation for the future, and a security that the books were carried forward from month to month in the state in which they should be audited. His remuneration was not very large, but it must not be taken to have been inadequate. He also must be taken to have had a knowledge of the business. It was not a business to which any of the directors could have been expected to devote anything like their whole time; and it was a business where, to Mr. Kevans' own knowledge, the clerical staff was cut down to a very low point. Therefore, he must have known that there was more reliance placed upon him, upon his checking, and upon the audit, than might be expected in the case of an ordinary company. That being the measure of his duty—it is the same rule that applies to all, with the exception I have mentioned—what is the nature of the breach of that duty? It is curious that in one English case the breach of duty for which the Auditor was said to be held liable was exactly as here—a breach of duty in not detecting the case of misfeasance on the part of others, which was not for the purpose of putting money into their own pockets, but for the purpose of giving a fictitious appearance of prosperity to a company that really was not prosperous. I shall have to say more about that when I come to the question of damages. I think the fairest way to deal with Mr. Kevans in this case is to treat him as being charged with having failed to find just cause of suspicion on the face of these books, which, if found, would have imposed on him the duty of pursuing his suspicion until he found whether it was or was not well founded; and in that I am only following the example of Lord

Justice Keane, who, in his judgment, took as an example one particular instance of one particular year, and applied all the rest of the case to that. I am fortunate in the present case to have an instance which was discussed as a fair example of the mode in which the fraud in question was carried out; as an example of the grounds of suspicion—that there were grounds of suspicion—appearing on the face of the books themselves; and also of the means that these books would have supplied (had the suspicion been entertained), in order to detect the frauds. Now, I must entirely disclaim from myself the intention of going to do anything more than what any ordinary intelligent juror would be bound to do if he was trying Mr. Kevans on his indictment for having failed to discover what appears on the face of the books themselves. This is not a question of technical knowledge, nor a question in which it could be capable of misleading anyone. The English cases have established that the Auditor is entitled, in the absence of the elements of suspicion, to assume that the books are honestly kept, and that, therefore, unless on the face of a presumably honest book something appears to excite his suspicion, he is not guilty of negligence, whatever other people might be in their departments, if he does not discover that something was wrong. Now, the one example is the case of Hill & Sons, for the period where the balance was struck as of the 31st of December 1892 and the 31st of December 1893. In that year there was an increase, as now appears, in the suppressed invoices and in the carried over invoices, and this account is one of those in which that increase took place, and it has been taken and discussed as an instance and as an example of others in the book (Creditors' Ledger), presumably dealt with in the same way. At page 108 of the Ledger the account of Hill & Sons—if I use a technical word wrongly I hope I may be forgiven—is ruled on the 31st of December 1892. The figures immediately below the ruling indicate to my mind that, when it was ruled, all the items for that year were then written up. From the 12th of August to the 20th of December 1892 there were, altogether, items that amount only to £57 3s. 9d., and all of these items are on the one date, December 20th. There were no transactions with Hill & Sons between the 12th of August and the 31st of December, except whatever is covered by the entries of the 20th of December. Therefore, if there was anything written in it could only be the £57 3s. 9d.; but I think it is admitted that these were not written afterwards, because after that, and the very last item above the ruling, is the correction of an error of £500, which is taken from the contra side of the account; and there is a ruling on the top of £736 4s. 9d., and there the account ends for the year 1892. On the face of the book there is no subsequent entry in Hill & Sons' account at all

going back into 1892. It is a perfectly legible account for 1892, closed on the 31st of December, balanced by the correction of an error, and, as I call it, closed in every sense. I will assume that all the transactions of 1892 were included in the accounts of 1892, and that there was nothing carried forward. Now, there is also a ruling on the 31st of December 1893—there is on the face of the book, as it stands, an undoubted ruling as of the 31st of December 1893. But what is the case? It is conceded that in striking a Trial Balance for the purpose of statements of account for the year 1893, three items that only appear on the right side of page 150 were in the book at the time. In the book now, before we come to the ruling, there were inserted below these and after them a half column of items totting to no less than £698 19s. 11d., and the whole of that is included in the amount of these “kept-back invoices” for the year 1893. Well, I will admit that it is not the business of an Auditor when he comes to strike his Trial Balance on the 31st of December for the purpose of a meeting, to have every account closed and balanced, but he must strike a Trial Balance, and he did so; but at a figure, 15th of December. I do not agree with the monthly check that was taken. Some of these items now introduced must have been there, and therefore within a month of the 31st of December 1893, if the monthly check had been carried out, the representative of Mr. Kevans would have found that after the figure which he had taken for ascertaining the financial position of this company, a string of figures had been put in, all in December, and all within a day or two of the 15th, the day at which the financial position of the company had been ascertained. I think that was something; but it is nothing to what follows, because between that time and whatever time this book was ruled there then follows a further string of items—nearly £600 in amount—that go up to the 3rd of November and go down as far as the 14th of December. I cannot conceive any more clear or glaring grounds of suspicion than to discover in the account of a single customer items amounting to such a sum having got into the books after the Trial Balance is struck under dates going back two months prior to the period of the ascertaining of the Trial Balance. There appears to be a further thing—a monthly check was to be adopted, and that would have put an Auditor on inquiry. It appears to me that the moment I come to the conclusion that that was on the face of it a suspicious mode of dealing with Hill & Sons’ figures, I am bound to show how it would be corrected. I can add nothing to the judgment of Lord Justice Holmes—viz., that it would then have been necessary to call for the creditors’ statements of account, and at that moment they would have disclosed on the face of them not merely those post-dated items, but the suppressed invoices also; and at the

instant that this discovery was made there is an absolute conviction of something wrong forced upon the mind of the Auditor. It, therefore, occurs to me that, upon these two branches, all that is required, both to show the negligence, to arouse suspicion, and to supply the means of putting a stop to the frauds, is to be found on the face of the book, and for all I have said I have no foundation except what is upon the face of that book (Creditors' Ledger). I now take the three English cases, in order to make a few observations on each. In 36 Ch.D., in the *Leeds Estate Building Investment Co.*, Mr. Justice Stirling held that the manager and Auditor were liable. It is right to say that the procedure in the other cases was different from this Leeds case; and it is important to bear in mind that the other two were under the 10th Section of the Winding-up Act. In this case the Auditor was held liable, and Mr. Justice Stirling held him liable, saying that it was his duty to see that no part of the capital was applied to any other than the proper purpose, and, in particular, that no part of the capital was returned to the creditors—that is, in dividends—except in the cases in which a reduction of capital was permitted by various Acts of Parliament. The next case, and the most important one, is the *London and General Bank* (2 Ch.D. 1895, 681). That was a procedure under this 10th Section. Mr. Justice Lindley says, "An Auditor has nothing to do with the prudence or imprudence of the way in which the business has been carried on; nothing to say as to whether it was properly, improperly, profitably, or unprofitably carried on, provided he discharges his own duties to the shareholders. His business is to ascertain and state the true financial position of the company at the time of the audit, and his duty is confined to that." But then comes the question, "How is he to ascertain that?" The answer is by examining the books of the company. But he does not discharge his duty by doing this without inquiry and without taking the common trouble to see that the books show the company's true position. He must take reasonable care to see that this is done (page 682), otherwise the audit reduces itself to an "idle farce." I have endeavoured to keep myself within that, and think that that principle is the very lowest upon which we can define the duties of an Auditor. In the *Kingston Cotton Mills* case (1 Ch.D. 96, 279), Mr. Justice Vaughan Williams held, "that it was the duty of the Auditor to have made a calculation outside the books which, if made, would have shown that the amount of the stock was overstated on the books." In this case of the stock-taking and the over-valuing, &c., Mr. Kevans is exonerated. Now, time after time, this passage about the "watch dog and the bloodhound" has been made use of, and I would wish to say a word regarding it, too. His Lordship then read from Lord Justice Lindley's judgment the passages dealing with the duties of Auditors, in one of which it was laid down

that "an Auditor was a watch dog, but not a bloodhound." This, Lord Justice Fitzgibbon remarked, was very unfair to the bloodhound, who was just as little likely to have his sense of suspicion aroused as the watch dog. Applying this instance of the dogs to the present case, was not the watch dog bound to bark? and if, when sniffing round, you hit upon a trail of something wrong, surely you must follow it up, and there is just as much obligation on the Auditor, who is bound to keep his eyes open, and his nose, too. As in the case of the hound, the Auditor will follow up this trail to the end, and the first things he will "root up" are those statements of account, and then the fraud is discovered. On the question of damages, the damage here—and I guard myself against expressing any individual opinion upon anything more than is necessary—is sufficiently supplied for the purpose of showing the existence of pecuniary losses. In the first place, there has been a paying away of a large amount of money in dividends to the shareholders that had not been earned, and therefore at the time that that was stopped the company ought to have been in possession of a money capital, which they had parted with by paying it away to their shareholders. It would be premature to discuss the pecuniary damage until the financial position of the company is finally ascertained. Then, again, had this system of the suppression—the carrying forward—of invoices been detected sooner, it would have been open to the directors to have done something to stop it. They had several ways, either to increase their percentages or diminish their dealings—in the latter case thereby producing a less loss; or, they could have stopped the business and wound it up. On the question of the amount of the damages, that depends on the amount of the losses the plaintiff has suffered, taking all the circumstances of the case into consideration. We have not all these circumstances before us, and it is, I say, premature to discuss damages at all beyond the point I have discussed them. I have come with much reluctance to the conclusion that a professional man has failed in his duty, and I am glad to be able to think that the worse that could be said of the case is this:—That, in what is so small a company, Mr. Kevans and his representative, who went there to do this audit (for which Mr. Kevans received a very small fee), were deceived not by any glaring or probable fraud such as they would be on the watch against, but by a thing that was done more for the purpose of giving an appearance of fictitious prosperity to a company which did not exist than that of putting money into the pockets of shareholders. That, however, cannot alter the legal liability if it is based, as I am satisfied it is, upon the failure to have suspicion aroused.

The Lord Chancellor also concurred, and the appeal was accordingly dismissed.

The case of MAYNARDS, LIM. v. MAYNARDS AND OTHERS.

(Decided before Mr. Justice FARWELL, in the Chancery Division, on the 16th January 1900.)

Company Prospectus—Alleged False Statements—Accountants' "Certificate" of Profits—Certificate merely an Estimate—Action against Promoters and Accountants for return of Money and Shares (or for Damages)—Promoters and Secret Profits.

In this case the plaintiff company, which was incorporated on March 19th 1896, for the purpose of carrying on a wholesale and retail confectionery business, alleges that certain of the defendants, who were promoters of the company, are liable to return money and shares to the company, on the ground that they made secret profits out of its formation, and that certain others of the defendants are also liable to return money and shares (or in damages) for having knowingly made false statements as to the profits, &c., of the businesses taken over by the company; which statements were embodied in the prospectus.

Sir E. Clarke, Q.C., Mr. Bramwell Davis, Q.C., and Mr. A. R. Kirby appeared for the plaintiffs; Mr. Swinfen Eady, Q.C., Mr. Hughes, Q.C., and Mr. Stewart Smith for Messrs. Oscar Berry & Carr; Mr. Younger, Q.C., and Mr. Buckmaster for Messrs. Edwards, Etherington & Willmott; Mr. R. Isaacs, Q.C., and Mr. Gregson for Mr. Thomas Maynard; Mr. Ashton Cross and Mr. Duka for Messrs. Edridge & Jackson; Mr. E. Ford for Mr. George Plumbley; Mr. H. E. Wright for Mr. Hatcher; and Mr. Parikh for Mr. F. C. Rhys.

Sir E. Clarke, in opening the case for the plaintiffs, said that before the incorporation of the company the defendant, Mr. T. Maynard, was carrying on business as a confectioner in sixteen shops in London. He put himself in communication with the defendant Mr. F. C. Rhys, and through him with the defendants Messrs. Edwards, Etherington & Willmott and Mr. George Plumbley, with the view of promoting a company; and all these defendants subsequently acted as promoters of the plaintiff company. Mr. Rhys concealed his identity under a company called the Home, Foreign, and Colonial Contract Company, which had only seven subscribers. The promoters decided to acquire a number of other businesses besides those of Mr. Thomas Maynard, and entered into contracts giving the option to purchase thirty-five other businesses carried on in different parts of England. At a later period Mr. Charles Riley Maynard, who was originally a defendant in the action, but with whom a settlement had been effected, agreed

to sell his six businesses in London to the intended company. On March 4th 1896, the defendants Messrs. Edridge, Hatcher & Jackson, who were trade valuers, made a report addressed to the directors of Maynards, Lim., although the company was not then in existence, in which they valued the businesses to be acquired by the company as a going concern (including goodwill, but exclusive of stock) at £72,500. and reported that they were satisfied that the net profits were then £15,000 per annum. This report appeared in the subsequent prospectus. On the same day the defendants Messrs. Oscar Berry & Carr, Chartered Accountants, furnished the following report to the promoters, but addressed to Maynards, Lim.:—"We have examined the accounts of the forty-six retail businesses proposed to be acquired by your company, the majority of which have been established for several years. The accounts show that the businesses have been steadily increasing, the sales now being at the rate of £39,542 7s. 5d. per annum. We have also examined the accounts of the wholesale businesses carried on in connection with these retail shops, and find that the sales are at the rate of £17,795 11s. 7d. per annum, of which by far the greater portion is for goods supplied to customers other than the retail businesses, the total sales of the combined retail and wholesale businesses above referred to being at the rate of £57,337 19s. per annum. Owing to the absence of figures showing the expenses of some of the businesses, we are unable to ascertain the exact net profit of the whole of them, but from our knowledge of the extremely profitable nature of the confectionery trade and from the facts disclosed during our investigation we are satisfied that the profits of the businesses are large, and that after payment of the interest on the preference shares there will remain a profit sufficient to pay a substantial dividend upon the ordinary shares." This report also appeared in the prospectus. As to these two reports, the plaintiffs would contend that Messrs. Edridge, Hatcher & Jackson never surveyed the premises in such a way as to enable them to form any opinion as to their value, and never, as the promoters knew, properly investigated the trading and were not satisfied that the net profits were £15,000 per annum; and that Messrs. Oscar Berry & Carr never had any materials before them, for they did not exist, for forming an estimate of the net profits. On March 9th 1896 an agreement was signed between Mr. Thomas Maynard and a Mr. Goodman, who was a nominee of the promoters, for the sale by Mr. Thomas Maynard to the company of his own business and thirty-five other businesses for £75,000, exclusive of the stock. Mr. Maynard appeared as the vendor of all the businesses in order that they might all have the benefit of his name and might appear to have been carried on by him. The capital of the company was £140,000, divided into 60,000 preference and 80,000 ordinary shares. On March 13 1896, the promoters issued a prospectus offering

52,500 preference and 60,000 ordinary shares to the public, and stating that the purchase-price was £115,000, which included £40,000 for Mr. C. R. Maynard's business, but no reference was made to the fact that any part of the purchase-price was to be paid to any of the promoters other than the ostensible vendors. The public subscribed largely for the shares. As a matter of fact £29,000 in cash and shares was paid to Mr. C. R. Maynard, £12,000 in cash and shares to Mr. T. Maynard, £33,200 in cash and shares to other vendors, and £44,484 18s. 3d. to or among the promoters and their nominees. The promoters also paid Messrs. Edridge, Hatcher & Jackson £350 in cash and £750 in shares. The price of Mr. C. R. Maynard's business was increased to and fixed at £40,000 in order that £11,000 might be secretly divided among the promoters. The profits of the company for the first year amounted to £2,714. A committee of shareholders was appointed, and after an accountant had investigated the various businesses which had been acquired, the present proceedings were instituted.

Mr. W. B. Keen, examined by Sir E. Clarke, said that he was a Chartered Accountant, and in September 1897 he was employed to examine the books of the various businesses taken over by the plaintiff company. There were fifty-one businesses in all, and the books varied greatly in character, and in no case was he shown a complete set. With regard to the profits of the businesses of C. R. Maynard, the certificate in the prospectus was correct. Sixteen of the businesses taken over belonged to Thomas Maynard, and with regard to these the books covered only a period of nine months, during which time there had been no stocktaking. The net profit for that period was £165 odd, and in his report he put the outside net profits at £365 per annum, without charging managerial services. For the first year of the company's existence the net profit from these sixteen businesses was £60 odd. The purchase-price was £15,000. The other businesses taken over belonged to different persons. In some cases no books were produced; in no case were they complete. In his report he put the total profits at £5,620, without allowing for managerial expenses, head office expenses, or depreciation. It was not correct to say, as was done in the prospectus, that the businesses were steadily increasing. In those cases where three years' books were produced to him the totals for the third year were less than for the first year. The method adopted by Messrs. Oscar Berry & Carr in estimating the net profits was, in his opinion, incorrect. The expenses of the different businesses varied greatly, and no fixed percentage could be realised.

Cross-examined by Mr. Hughes: I am aware that Messrs. Oscar Berry & Carr declined to certify as to net profits.

Witness was also cross-examined by Mr. Ashton Cross, Mr. Younger, and Mr. Parikh.

To Mr. Justice Farwell: Mr. J. J. Clark, of Brighton, was the only vendor who kept proper books, but in no case were books produced to me from which an accountant could arrive at a correct conclusion as to net profits.

Mr. Francis William Pixley, examined by Sir E. Clarke, said he was a member of the Council of the Institute of Chartered Accountants. There had been submitted to him certain documents which, he understood, had been supplied by Messrs. Oscar Berry & Carr to the last witness (Mr. Keen) for the purpose of showing how their figures had been arrived at when they reported that the accounts of the businesses showed increasing profits, sufficient to pay a substantial dividend on the ordinary capital after paying the dividend on the preference shares. It was not the fact that those accounts showed that the businesses had been steadily increasing. There was only one document dealing with Maynard's businesses at Brighton, and it covered only one single year, so it could not show whether the businesses had been progressive; but the books appeared in this case to have been correctly kept. In other cases the figures were only for one year; so that they did not show whether there had been an increase or decrease. Figures for 1893, 1894, and 1895 were given in other cases. In Stewart's case the takings in the first year were £4,676 17s. 3d., in the second year £4,122 6s., and in the third year £3,830 11s. 10d., showing a decrease in each year. In Vose's case the figures were £5,613 9s., £6,280 0s. 6d., and £6,280 4s. 7d. respectively, being an increase each year. In Jarvis's case the figures were £2,423, £2,490, and £2,325 respectively. Having regard to the whole of the figures shown to him, there was no justification for saying that these were progressive businesses. There was nothing in the documents produced to him to justify the statement by the trade valuers, Messrs. Edridge, Hatcher & Jackson, that they were "satisfied that the net profits were upwards of £15,000 per annum."

Cross-examined by Mr. Swinfen Eady: A person knowing the trade could form an idea, from the turnover, of what profit ought to be made. If a large number of shops were amalgamated, and conducted under a central management, the profits would be greater than if the businesses were carried on separately. The fee of 700 guineas to Oscar Berry & Carr was, he would say, a full fee, but not excessive for the work.

Mr. Frederick Whinney, examined by Sir E. Clarke, said he was an accountant in the City, and had practised for forty years. He had

seen the certificates of the valuers and the accountants in the prospectus, and had had the papers submitted to him which had been shown to the previous witness. They suggested a profit of between £14,000 to £15,000 a year; but he did not think they could be depended upon, because they were not based on accounts. They were estimates. He did not believe in estimates at all, and if one was giving a certificate, if he could not get real information, he ought to state that he had been obliged to estimate so-and-so.—Was there anything in the documents which would entitle a person to say he was satisfied that the net profits amounted to £15,000?—Witness: I would not have said so, and I do not think anyone else ought to have said so.

By Mr. Hughes: He did not know that Oscar Berry & Carr declined to certify the net profits.—Mr. Hughes: They said they were unable to ascertain the exact net profit, but that from their knowledge they anticipated, besides the 6 per cent. on the preference shares, a substantial dividend for the ordinary shares. There is no mention of £15,000, or any sum, by Oscar Berry & Carr?—Witness: But you find it inferentially.

Mr. Herbert Furber, examined by Mr. Kirby, said he had examined most of the shops scheduled in the prospectus. Some of these were held on yearly tenancy, others on leases averaging twelve and a half years. He did not value the goodwill of those held for a year or less, and his valuation of the goodwill of the others was £4,065.

Mr. William Izard, auctioneer and trade valuer, in answer to Mr. Kirby, said that he had had special experience in the valuation of confectionery businesses. Apart from factories, he had inspected over forty of the shops of this company in London, Brighton, and elsewhere, and he valued the leaseholds at £3,750 and £700 for a shop in Newcastle. In his opinion, there was nothing to be added to those figures for goodwill.—By Mr. Ashton Cross: He had put no value at all on any of the company's shops that had been shut up. It was his experience that confectioners commonly bought and sold without proper books, and businesses were bought and sold often only upon estimates.

Mr. John Jackson Clark, examined by Sir E. Clarke, said he carried on confectionery businesses at Brighton under the name of Maynard, and he had lately joined the board of directors of the plaintiff company. Mr. Rhys communicated with him as to the purchase of his businesses. He gave Mr. Rhys no accounts regarding the factory, as he told him it was no good, and he gave Oscar Berry & Carr the same information. He had said all along that he was only selling the good-

will of the retail businesses; there was no goodwill of the others. Rhys only had witness's statement, but a clerk of Oscar Berry & Carr came and examined the books for the year 1894. The books went back to 1888, but he did not know whether the clerk examined beyond the year 1894.

Mr. C. R. Maynard, examined by Sir E. Clarke, said that he was managing director of the plaintiff company. Early in 1896 he came into communication with Mr. F. C. Rhys, and on March 14 of that year signed an agreement with Mr. Goodman on behalf of the company to sell his business to the company. The consideration was £40,000, £25,000 to be in cash and £15,000 in shares. He received £14,000 in cash out of the £25,000, and was allotted 15,000 shares, half preference and half ordinary. Messrs. Edwards, Etherington & Willmott, and Mr. G. Plumbley received £10,000 of the nominal consideration money in accordance with an understanding he had entered into with them. He obtained an indemnity in exchange for them; £1,000 of the consideration money went to Mr. Rhys, but he did not know under what circumstances. In April 1897, he valued plant, machinery, and fixtures acquired by the company. He thought the valuation was between £16,000 and £17,000. That included businesses acquired after the promotion of the company.

Cross-examined by Mr. Swinfen Eady: The directors issued a circular criticising Mr. Keen's report, and he believed those criticisms to be well founded. He visited all the shops before completion of the purchases and reported on them, and he understood that two of the directors had also done so.

Cross-examined by Mr. Parikh: Mr. Rhys might have settled the costs of witness's solicitors and the accountants' costs out of the £1,000 that went to him.

Mr. E. R. Polden, chairman of the plaintiff company, said, in answer to Sir E. Clarke, that he was a director of a printing business, and had done a good deal of printing in connection with companies promoted by Messrs. Edwards, Etherington & Willmott. Mr. Edwards first introduced this business to him, and he agreed to underwrite 2,000 shares. Mr. Edwards afterwards suggested that he should become a director, and he agreed to this. About March 1896, Mr. Edwards gave him £100, but he considered that it was given as a present for the personal trouble he had taken in looking after the printing for Mr. Edwards's firm. It was about the same time that he applied for 100 shares in the company to qualify him as a director. He never saw

Mr. Rhys nor heard of Mr. Plumbley till afterwards. He did not know that Messrs. Edwards, Etherington & Willmott, and Mr. Plumbley were to receive £21,000 out of the sum paid to Mr. T. Maynard. He did remember a conversation with Mr. Edwards, in which £30,000 was mentioned as the profits and costs of the promotion of the company. Had he not believed the statements in the prospectus he would not have become a director.

Cross-examined by Mr. Isaacs: He knew before completion that Mr. T. Maynard was not the real vendor of all the businesses.

Cross-examined by Mr. Swinfen Eady: The directors did not act in accordance with the directions of the promoters.

Re-examined by Sir E. Clarke: He paid £100 to the committee of investigation, but without any admissions, in order that action against him might be stayed.

Mr. Bramwell Davis summed up the evidence for the plaintiffs, and said that the plaintiffs claimed that the defendants were liable to return to the company the difference between the actual value of the businesses sold to the company, which was between £16,000 and £17,000, and the price paid for them, £75,000.

Mr. Rufus Isaacs, on behalf of Mr. T. Maynard, contended that the directors knew from the beginning that Mr. T. Maynard was not the real owner of all the businesses acquired by the company. His client had done nothing which was not disclosed to the directors and, through them, to the company. There was no evidence of complicity against him with regard to the prospectus, and as he had nothing to do with the promotion he did not stand in any fiduciary position towards the company. All that was suggested against Mr. Maynard was that, owning only sixteen shops, he purported to be the vendor of the rest.

Mr. Swinfen Eady said that the charge against his clients, Messrs. Oscar Berry & Carr, who held a high position in their profession, was either fraud or nothing. There was no question of contract with the directors, because their report was furnished before the company was formed. The allegations made against his clients were wholly false, and the fullest evidence would be given to prove that. For the purposes of the report Messrs. Oscar Berry & Carr examined fifty-one businesses in all, and their fee was to be 700 guineas. It was subsequently arranged that part of the fee should be paid in shares of the company. Mr. Bramwell Davis had said that the plaintiffs' claim against the

defendants was for £60,000, the difference between the value of the businesses, as assessed by the plaintiffs, and the price paid. But while the action was pending, the plaintiffs' solicitors had written a letter to his clients' solicitors saying that their claim was not for fraudulent misrepresentation of the value of the businesses acquired by the company, and on that ground they refused discovery of certain documents. Therefore, so far as his clients were concerned, the plaintiffs' claim for £60,000 must fall to the ground.

Mr. Justice Farwell: In face of that letter, Mr. Bramwell Davis, I do not quite see how I can give you leave to amend your claim. However, perhaps it will be better to hear the evidence.

Mr. Swinfen Eady: The evidence would prove that Messrs. Oscar Berry & Carr had acted solely as accountants in the matter, and had no motives for acting otherwise. They were asked to investigate certain businesses and certify as to profits. As the materials were not sufficient they declined to certify as to profits. They were then instructed to ascertain the amount of the takings, which could be done with fair accuracy. Given the takings, a person of experience could then compute what the profits were likely to be—substantial or otherwise. It was true that when the company took over the businesses the net profits fell off, though the takings increased. He hoped, however, that his evidence would show where the leakage took place.

Mr. W. R. T. Carr said, in answer to Mr. Swinfen Eady, that he was partner in Messrs. Oscar Berry & Carr and had had a long experience as an accountant. The investigations into the businesses acquired by the plaintiff company were conducted under his personal supervision. He was told the fee was to be 700 guineas. Before the certificate was given he had never heard that part of the fee was to be paid in shares, or that payment was conditional on the company being successfully floated. They examined fifty-one businesses in all—forty-six retail and five wholesale. They went through the accounts of ninety-five years. They were instructed at first to certify as to net profits, but the net profits could be ascertained from the books of only twenty of the businesses. This was told to Mr. Rhys, and they were then instructed to ascertain the sales, which they did. Mr. Gold, one of the original directors, was also informed that they could not certify as to net profits. In a great many of the businesses their investigations covered a period of three years.

Witness then went at great length into the details of the accounts taken by his firm with a view to proving the accuracy of their report.

In answer to Mr. Swinfen Eady, witness said that he still retained the shares in the plaintiff company which were given in part payment of

the fee of 700 guineas, though he had been twice approached to sell them. The shares went to a premium. Under the company the turn-over of the businesses largely increased, but the net profits fell off.

Cross-examined by Sir E. Clarke: He should not like to say that the accounts he examined would support the statement in the prospectus that the profits were sufficient to pay 15 per cent. on the ordinary shares. He did not consider his report as a certificate of net profits. When he saw the prospectus he did not remonstrate with the directors as to any statements in it. It was by Mr. Rhys's instructions that he addressed the certificate to the directors. Out of the forty-six retail businesses thirty-five had accounts sufficient to enable him to give the profits approximately.

Witness was then cross-examined at great length on the accounts of the various businesses acquired by the company, with a view to proving the allegations of the plaintiffs that the businesses were not increasing at the date of the certificate, and that there were no materials sufficient to allow profits to be estimated.

Mr. Edridge, examined by Mr. Ashton Cross, said that he was a member of the firm of Edridge & Jackson, which at the date of their certificate was Edridge, Hatcher & Jackson, and had had a long experience as a trade valuer in the confectionery and allied trades. Together with his partner, Mr. Jackson, he inspected the various leasehold premises in London, Bristol, Bath, and Brighton acquired by the company, and valued the fixtures and fittings. Mr. Jackson inspected the businesses in the North of England. The values were entered in books on the spot, and all the valuations were honestly made. Confectioners seldom kept complete sets of books, and in such cases it was usual for valuers to inspect the shop, ascertain rates and taxes and other details, such as number of assistants, class of trade, competition, and character of management. A valuer of experience could then form a pretty good estimate of the amount of trading, and by that process the net profits could be approximately arrived at. They had gone through that process in the present case, and honestly satisfied themselves as to the amount of the net profits.

Cross-examined by Sir E. Clarke: They depended on Messrs. Oscar Berry & Carr for the correctness of the takings. He still believed that the net profits were £15,000 per annum at the date of his report.

Mr. S. P. Jackson, examined by Mr. Duka, confirmed the evidence of the previous witness.

It was notified that the case against Mr. Thomas Maynard had been settled.

Mr. F. C. Rhys, examined by Mr. Parikh, said that he held in 1895 contracts for the purchase of certain confectionery businesses, and entered into negotiations with the Home, Foreign, and Colonial Contract Company for the transfer of the contracts to that company. He had no other connection with the Contract Company. Ultimately he employed that company as his agents to dispose of his contracts, which they did. He had taken no part in the formation of the plaintiff company. The directors knew that certain cash and shares were given to him, his name being on the nomination.

After Mr. Younger and Mr. Parikh had addressed the Court on behalf of their respective clients,

Sir E. Clarke said that the plaintiffs did not ask for judgment against Mr. Rhys, and that it had been settled that judgment should be entered against Messrs. Edwards, Etherington & Willmott for moneys received from the company and not accounted for. He wished it to be understood that all charges of fraud against Messrs. Edwards, Etherington & Willmott were withdrawn.

Mr. Ford, on behalf of Mr. George Plumbley, contended that all his client received was a fair remuneration for the trouble and risk of promoting the company. The directors knew he was receiving money, so that his profits could not be called secret.

JUDGMENT.

Mr. Justice Farwell: I am convinced that Messrs. Oscar Berry & Carr and Messrs. Edridge, Hatcher & Jackson acted quite honestly, and were honestly satisfied of the correctness of their reports. Nor am I satisfied, though that is not the issue I have to try, that their reports were not substantially correct. The plaintiffs have brought charges of fraud against these defendants, and those charges having failed I see no reason to depart from the usual rule as to costs. The action as against Messrs. Oscar Berry & Carr, Messrs. Edridge & Jackson, and Mr. Hatcher must consequently be dismissed with costs. The case had been disposed of as against all the defendants except Mr. Plumbley. He had already stated that the charges of fraud against Messrs. Oscar Berry & Carr and Messrs. Edridge, Hatcher & Jackson had broken down, and he would now reiterate his belief that those gentlemen had acted in the matter with honesty and integrity. As to Mr. Plumbley, he was admittedly a promoter. It had been argued that as the directors knew of the payment to him that amounted to notice to the company, and the company, consequently, could not sue. In his opinion, however, in a matter of this nature notice to the directors did not bind the company. The directors were not agents of the company to pay money beyond the purchase-money. Mr. Plumbley must, therefore, be held liable, and, as Sir E. Clarke had intimated that what the plaintiffs

now claimed was £16,000, there must be judgment against Mr. Plumbley for that amount, with liberty for him to set off whatever sums were recovered, in accordance with the various settlements of the case, from the other defendants. That judgment would not, however, carry costs, as the charge of fraud against Mr. Plumbley had broken down.

(*Acct. L.R.*, 1900, p. 24.)

The case of JOSEPH HARGREAVES, LIM.

(Decided before Mr. Justice COZENS-HARDY, in the Chancery Division,
on 15th February 1900.)

Held that an Auditor who refuses to Certify the Accounts of a Company cannot be held liable because no correct Accounts were submitted to the Shareholders.

In this case a summons was taken out by the voluntary liquidator of Joseph Hargreaves, Lim., asking the Court to hold three directors and the Auditor of the company liable for misfeasance in having declared dividends, amounting to £2,602, out of capital. The directors who were respondents to the summons were Messrs. Pullen, Holloway, and Brown; and the Auditor was Mr. Theodore Brook Jones, Chartered Accountant, of Albion Street, Leeds. The company carried on business as spinners at Shipley and Bradford, and the allegation against the respondents was that in 1894 and the two following years dividends were declared when the company had really made no profit. The company had passed resolutions for voluntary winding up in August 1897.

Mr. Hughes, Q.C., and Mr. Percy Wheeler appeared for Mr. Gray, of Bradford, the liquidator; Mr. Eve, Q.C., and Mr. R. J. Parker represented Mr. Jones; and Mr. Astbury, Q.C., and Mr. Stewart Smith were counsel for Mr. Pullen. The other directors were not represented.

The affidavit of Mr. Jones was read by Mr. Eve. The deponent stated that he had never received any remuneration from the company, and he had not acted as Auditor after the 22nd of June 1895. A valuation of the machinery had been made by Mr. Marshall in 1894, and that gentleman had arrived at a figure of £16,119, with an addition of 10 per cent. owing to the marked improvement in the textile trade.

Mr. Jones was cross-examined by Mr. Hughes. He said he saw to the preparation of the memorandum and articles of association, and he gave all the information he could to the shareholders at their first meeting. He knew that certain sums were paid to the shareholders as dividend, but when he found no profit had been made he refused to sign the Balance Sheet. He several times spoke to Mr. Holloway on the subject, but nothing was done. He denied that he concurred in any resolution that any sum should be carried forward. Witness was not re-appointed Auditor in December 1895, but his firm acted as

Auditors more through friendly feeling towards the directors than anything else. He never received a penny as remuneration, and had never sent in an account, though one of his clerks, contrary to instructions, had sent in an account to the liquidator. He acted as much in the shareholders' interest as in the directors', but he did not report to the company in general meeting. He more than once protested to Mr. Holloway that dividends were paid before the accounts were audited. He could swear positively that there were no Balance Sheets signed by him or on his behalf. Dividends had been paid to him in respect of the shares he held in the company.

Re-examined: I told the directors that they were liable for the dividends which had been paid out of capital.

Mr. Stewart Smith read the affidavit of Mr. Pullen, to the effect that that gentleman up to the formation of the company had been general manager of Mr. George Hargreaves' mills, Holloway was cashier, and Brown salesman. After the company was formed they continued to work in their own departments. He never had brought to his notice the objections to the accounts which the Auditor made to Mr. Holloway. He did not, however, dispute his liability in respect of such dividends as had been paid out of capital. The learned counsel desired to say that Mr. Pullen was the holder of only 250 ordinary shares in the company, on which there had never been any dividend paid, and he had never received a shilling out of the company in which he had sunk all his money.

His Lordship asked if the liquidator would be content with an order for the payment of the 1896 dividend only.

Mr. Hughes desired to be moderate, and said he would take an order that the directors were jointly and severally liable in respect of £1,177. As regarded the Auditor, he argued that it was a plain case of neglect of duty against him, as he should either have brought the matter to the knowledge of the shareholders or he should have resigned.

JUDGMENT.

Cozens-Hardy, J.: In this case I have made up my mind—so far as the directors are concerned I need not say any more as to them. The question remains as between the liquidator on the one hand and the Auditor on the other. It is sought to make the Auditor liable for three dividends paid out of capital, and it is sought to make him liable under circumstances the like of which, so far as I am aware, have never occurred before. Mr. Jones has never signed any Balance Sheet; no resolution of the company or of the directors has ever been passed for the payment of a dividend; nothing has ever been done by the directors, or by anybody, on the footing of any inaccurate statement, insufficient statement, or dishonest statement, by Mr. Jones. Mr. Jones told the

directors that, in his opinion, the payment of the dividend which had been made before the first audit was improper, because that was only justified by reason of an appreciation of the value of the machinery, which appreciation, assuming it to be proper, ought not in Mr. Jones's view to have been carried to the credit of Profit and Loss, but ought to have been carried to a Suspense Account, unless and until the shareholders' general meeting otherwise resolved. Mr. Jones for that reason deliberately refused to sign the Balance Sheet. No general meeting was called after that. That is the result of the evidence which is before me, and there is not a particle of evidence that any such general meeting ever was called; and Mr. Jones's duties, as defined by the articles of association, are first of all to examine and ascertain the accuracy of the Profit and Loss Account and Balance Sheet, and to report to the company in general meeting upon it. He could not, and would not, certify the correctness of this Balance Sheet, and I think he was perfectly right in refusing to do so. He did not report upon it to the general meeting for the best possible reason—that there was no general meeting to which he could report; and it is sought really, I think, when one gets to the bottom of the case, to render the Auditor liable because he did not require a general meeting of the shareholders to be summoned, to which he could make a statement as to the improper conduct of the directors. Well, how could he have summoned a meeting? He had no more power to summon a meeting than I have. I think, in Table A, five shareholders, I think it is—but never mind what the number is—can call a general meeting. But he could not call a general meeting. He did remonstrate with the directors and suggest that they should call a general meeting, but they did not do so. Now, these dividends in each of the years were paid out of the bank of the company without any resolution of the shareholders in general meeting, without even any resolution of the board of directors at a board meeting, and in each and every year the payments which are said to be, and which for the present purposes are assumed to be, improper were actually made before the audit of the accounts was completed. It would be startling, I think, to say that an Auditor who knows that dividends have been improperly paid out of capital is to be rendered liable because he does not commence an action on behalf of himself and all the other shareholders, I suppose, against the directors who have improperly paid these dividends, or does not do that which he really had no power to do—get the general meeting together and inform them of the facts. I think the duties of an Auditor are accurately, and, I might almost say, exhaustively, defined by Lord Justice Lindley in the *London and General Bank* case: he must be honest; he must not certify what he does not believe to be true; he must take reasonable care and skill before he believes that which he certifies is true. I think Mr. Jones has fully

come up to that definition. Certainly, as far as I am concerned, I am not prepared to extend the liabilities and responsibilities of Auditors to the enormous extent to which I should be obliged to extend them if I agreed with the present application. I think, therefore, the summons must be dismissed with costs as against Mr. Jones. The order will go with costs against the three directors. For the last year, the 1896 dividend.

Mr. Wheeler: And interest as asked by the summons from the date of payment?

Cozens-Hardy, J.: Yes; that would be a matter of course, I suppose.

Mr. Wheeler: That is asked by the summons.

Cozens-Hardy, J.: Of course, your costs and what you pay will come out of the assets of the company. It was quite a proper case to bring before the Court.

(*Leeds Mercury*, 16 February 1900.)

The case of GRIFFITH v. BRIGHTON HOTELS, LIM., and OTHERS.

(Decided before Mr. Justice RIDLEY and a Special Jury, in the Queen's Bench Division, on 22nd June 1900.)

Held that when a liability for Misfeasance exists, it is not got rid of by merely renouncing Fees due from the Company.

The plaintiff Mrs. Isabel Griffith, a widow, claimed on behalf of herself and all other the shareholders of the defendant company that the other defendants should be ordered to pay to the defendant company the sum of £394 19s. 4d., fraudulently and improperly paid away out of the defendant company's funds as dividends or damages for misfeasance and negligence. It appeared that the defendant company was incorporated on December 9 1897 for the purpose of carrying on certain hotels in Brighton, with a capital of £100,000, divided into 50,000 preference shares of £1 each (of which the plaintiff held 300), and 50,000 ordinary shares of £1 each. It was alleged that in August 1898 the defendants Parsonage, Prickett, and Coulson, as directors, ordered, and, on September 1 1898, caused the sum of £394 19s. 4d. of the company's money to be paid away as dividend to the preference shareholders, of which sum the defendant Parsonage received £40 6s. 5d. It was further alleged that there were no profits out of which this sum could be paid as dividend, but that, on the contrary, the trading had been carried on at a heavy loss, and that the defendant directors either knew these facts or negligently omitted to inquire into them before declaring and paying the dividend. Of

this sum of £394 19s. 4d., the plaintiff had received and returned £8 11s., and was now claiming the balance on behalf of the shareholders. The defendant Parsonage pleaded that one Armstrong, a banker and promoter, who was interested in and controlled the promotion of the Brighton Hotels, Lim., sent to the company a sum of £394 19s. 4d., and directed the directors to pay the interest on the 5½ per cent. cumulative preference shares, that this was interest and not dividend, and was paid by Armstrong and not by the company, though Armstrong afterwards charged the company with the repayment of the sum. He further pleaded that at the annual meeting of the company, held in June 1899, after the defendant had resigned his position as a director, the shareholders by resolution agreed to sanction the repayment to Armstrong of the sum of £394 19s. 4d., provided the directors would forego their claims to fees then due, which the directors then and there agreed to do. He further alleged that if the plaintiff held shares, she did so for Armstrong. The defendant Coulson pleaded that, if he had caused the payment of the alleged sum, he did so in the belief that profit to that amount had been earned, and acted *bonâ fide* and without negligence. The defendant Prickett entered a similar defence, and further pleaded that, of the sum distributed as dividend, £93 os. 10d. was properly received by him in respect of £3,500 preference shares held by him, and that he had returned it to the company, and had paid a further sum of £93 os. 10d., making a total of £186 1s. 8d. It was admitted, on behalf of the plaintiff, that the sum now owing was reduced to £200 6s. 8d.

Evidence having been given in support of the plaintiff's case,

Mr. Edmondson, on behalf of the defendant Parsonage, contended that the real plaintiff in this case was Mr. Armstrong, the banker, who, owing to Mr. Parsonage's investigations as chairman of the board, had been compelled to disgorge 10,500 shares in the company to which he was not entitled, which would form the subject of inquiry in another action. Mr. Parsonage had, in consequence of his discoveries, resigned his position. The company had not lost a penny owing to the declaration of the dividend, even if it ultimately came out of the capital, as the directors had agreed to reimburse it by foregoing their fees.

His Lordship expressed an opinion that this action of the directors could not be set off against the payment out of capital. The fees might have been foregone even if no such incident had occurred. Mr. Parsonage said he was induced to join the board by Mr. Armstrong.

He was chairman of it for about fifteen months, and during that time discovered that it was "a fraud from end to end." In August 1898 he was informed by a clerk of Mr. Armstrong's that Mr. Armstrong wished the interest on the preference shares to be paid. He replied ~~that~~ he had no personal knowledge as to whether there were profits, but subsequently the directors agreed to pay the dividend, Messrs. Armstrong & Co. advancing a large portion of the money. They afterwards discovered that no profits had been earned, and he voluntarily gave up his fees, the other directors arranging to do so, too. He resigned his position in July 1899.

In cross-examination the witness said he was a wine and spirit merchant, carrying on business as managing director of a limited company—Parsonage & Co. He agreed to subscribe for 2,000 preference shares in the Brighton Hotels on condition of having a seat on the board and the exclusive supply of the wines and spirits for five years at market value. He knew it was his duty to look after the shareholders' interests.

Mr. Isaacs: Does it not strike you that they might have got their wines and spirits better and cheaper elsewhere?

Witness: Impossible.

His Lordship: I am sorry I did not know that. (Laughter.)

Witness, continuing, said he did not, at the time, think it his duty to find out whether there were profits before the dividend was paid. Mr. Armstrong had brought him into the board, and he thought he was an honest man. There was not, when the dividend was paid, sufficient in the bank to pay. It was the slack season. He knew that, by the articles, they were only entitled to pay dividends out of the net profits. He was misled by Armstrong. He had not an exclusive interest in the wine and spirit company, to which the proportion of dividend was paid. The Balance Sheet of the Brighton Hotels, Lim., was not made out till June 12 1899, and was then a revelation to him, disclosing a loss. He found himself in the wrong, but considered he had repaid the company by giving up his fees for work done. He was not a seller of his shares, and the increased value of them as the result of the declaration of dividend was nothing to him. He relied on the statement of Armstrong that profits had been earned regularly in the past. He did not at the time know that Armstrong was a promoter, or that his statements as to the past profits were false. Before paying the dividends Armstrong's clerk assured him that, as regards profits, "it was all right and the dividend must be paid." He admitted he was wrong in paying the dividend, but contended

that he had paid it back by foregoing his fees. He resigned owing to "a projected cooking of accounts" to do away with the loss. He got up and left the board meeting, and sent in his resignation forthwith. The minute saying that he resigned "owing to pressure of business" was incorrect. He had never drawn any fees.

Re-examined: The contract that his company should exclusively supply wines and spirits was made public. He had never sold any of the shares.

Mr. Bayne, late secretary to the company, said that he was present at a meeting of the shareholders in June 1899. Mr. Prickett explained that there was a loss and that the directors would forego their fees. The report, which said that it was hoped "the shareholders would appreciate the sacrifice they had made," was adopted. Armstrong controlled the company. He (witness) was dismissed for demanding the return of £6,000 owed by Armstrong to the company. Armstrong, whose clerks were on the board, "shut him up" when he attempted to explain, and he was described in the minutes as dismissed "for gross misconduct."

Counsel having addressed the jury, his Lordship summed up, and left it to the jury to say whether an agreement was arrived at between the defendants and the shareholders that they should be released from liability for acting *ultra vires* in consideration that they renounced their fees.

The jury returned a verdict for the plaintiff for £200 6s. 8d. against the three defendant directors, and judgment was entered accordingly, a stay of execution being granted.

(*Times*, 23 June 1900.)

The case of DUMBELL'S BANKING COMPANY, LIM.

(Decided before a Special Court, held at Douglas, Isle of Man, on 5th to 14th November 1900, Lord HENNIKER presiding, assisted by Mr. H. GORDON SHEE, Q.C., of Salford, and Deemster MOORE.)

Prosecution under Manx Criminal Code 1872, Section 221 (identical with the Larceny Act, 1861, Section 84).

In this case Charles Banks Nelson, 53, a Ramsey advocate by profession, and a director of the bank; John Shimmon, 55, manager and secretary; Joseph Drake Rogers, 58, the Insular Auditor; William Aldred, 76, and Harold Vincent Aldred, 33, Chartered Accountants, Booth Street, Manchester, the English Auditors of the bank, were placed on their trial charged with issuing false Balance Sheets, knowing them to be false, and with intent to deceive.

Deemster Moore read the indictment to the effect that the prisoners were charged that they jointly did make, circulate, and publish, and concur in making, circulating, and publishing, three Balance Sheets, dated June and December 1898, and June 1899, which they knew to be false in material particulars, with intent to deceive and defraud the members, shareholders, and creditors of Dumbell's Banking Company. There were, said the Deemster, several other counts in the indictment varying in extent.

To a question from his Honour, all the prisoners pleaded not guilty.

Opening the case for the prosecution, the Attorney-General said the defendants were charged with a series of offences in contravention of Section 221 of the Manx Criminal Code of 1872. Happily such serious offences were rare, this being the first prosecution of the kind under the statute. He recalled the fact that Dumbell's Banking Company was incorporated in 1874 with a capital of £150,000, of which, however, only one-third was and could be by law called up. Article 6 of the company provided that no advance should be made to any director or officer of the bank without the consent in writing of the board of directors, and succeeding articles laid it down that the explicit duty of the Auditors was to distinguish in their reports between good, bad, and doubtful debts. The learned counsel pressed this strongly on the attention of the jury, but said they must not suppose he was implying that failure of duty was sufficient to constitute criminal guilt on the part of the defendants. Nothing of the sort. The Crown took upon itself the full burden of proving that they published these Balance Sheets knowing them to be false, and with intent to deceive all who were interested. Let them deal, in the first instance, with hard facts. It was provided that as soon as the bank had gone £50,000 to the bad, the shareholders should be called together, and the whole state of affairs submitted to them. In the Balance Sheet dated June 30 1898 it showed the item Cash-in-hand was alone false to upwards of £80,000, for it included £15,000 of the bank's own notes being dormant there, and £65,000 from the London City and Midland Bank, which was a mere figure of loan limit which had been agreed to. This item was purely fictitious, and represented no cash in hand at all, for at that very time Dumbell's owed the London bank over £89,000, and the next half-year £101,047. Yet in every one of the Balance Sheets that £65,000 and the uncirculated notes were put down as ready cash. Putting it briefly, the assets and liabilities were falsely given to the extent of £180,000 on the first and second Balance Sheets and £200,000 on the third. Had a true Balance

Sheet been published the bank could not have kept open one hour. The £65,000 was at last disposed of just prior to the bank suspending payment by Shimmon instructing a clerk to give credit for the amount to the London Bank, remarking it would be better to show their true position. Letters were read showing that considerable pressure was put on Dumbell's two managers by the general manager of the London City and Midland Bank, who, in June last year, pointed out that there was then owing £113,562, that never again would they be allowed to go such lengths, and finally he gave warning that they must be prepared for the stopping of all remittances and cheques. The learned Attorney proceeded to state that on the first Balance Sheet, out of £924,131 current advances and bills discounted, £234,764 were bad and irrecoverable to a very large extent, being due by people dead and bankrupt many years. One estate indebted to Dumbell's £17,000 would yield 1s. 9d. in the £. It practically amounted to this. Another tradesman, whose indebtedness when the bank closed was £24,339, would pay 4s. The average increase of withdrawals over payments amounted in the first case for six years to £1,590 a year, and in the second to £2,913 a year. A Peel tradesman had an overdraft of £21,853; his securities amounted to £550, and the estate would pay 1s. 5d. in the £. He drew out £1,800 a year more than he paid in. Another Peel tradesman had a debit balance of £17,000. He paid in between £300 and £400 a year, but drew out £1,500; his assets were £291, and his estate would pay 8d. in the £. These were fair samples, and a few only of the accounts on which all these people had been made bankrupt. Practically it amounted to this, that they had been living on the bank for years. Turning to the accounts in Nelson's name, counsel said the jury would require to deal with them in a distinctive manner. His total indebtedness to the bank was £71,984 13s. 4d. He had been made a bankrupt, and his assets were worth about £10,000. Nelson's own estimate was £20,000. Since 1896 he had gone to the bad at the rate of £8,000 a year. Some of the accounts were opened under circumstances which showed a want of *bona fides*. They were for speculative purposes, and Nelson had admitted to the liquidator that one account for £20,051 was to cover losses in Allsopp's shares, and that he, Shimmon, and Bruce, were equally liable. Shimmon denied any liability, but counsel would show that shares were made out in his name, that he wrote to the Ramsey agent authorising him to let Nelson open a new account, and otherwise participated in certain joint transactions. Nelson had always been perfectly candid with the liquidator regarding these various triple accounts. His general account

since 1896 had gone to the bad at the rate of £8,000 a year, rising from £7,800 to £39,000. The first joint cheque was drawn on the 7th of April 1887, and three joint accounts, amounting to £36,000 had been practically dead since 1893, no interest or payment in having been made upon them. In December 1898 the total bad debts amounted to £243,000, but in June 1899 they were £281,000, an increase of £38,000. Only a portion of these were included in the indictment. The reserve fund stood at £40,000 for years, and the inner contingency fund at £34,000. He would show that neither of them existed. The net balance of profit stated for the first half-year in 1898 was £5,370, but he would show that £5,174 of this was interest charged on dead and irrecoverable overdrafts, and that during the last half-year, while the profit was said to be £5,395, over £5,964 was charged as interest in the same manner, and £1,575 was interest accrued on Nelson's accounts alone. During all this period Dumbell's was paying 18 per cent. dividend, absorbing £4,500. Whatever might be Nelson's defence regarding the large unsecured overdrafts, he had, at least, knowledge of his own enormous overdrafts, and knew they never came before the board. Shimmon had been in the bank since he was a boy, and documents which were read linked him, said counsel, to a full knowledge of the facts. So far back as 1885 the Aldreds called attention to certain accounts, and in July last year wrote two letters to Shimmon, who answered them, advising the management to get security for some of these large overdrafts, and threatening to resign. A few days later Rogers wrote to the late Mr. Bruce in the same strain, and enclosed a list of overdraft people whom he considered bad, but who were included as good, amounting to £139,000, and later on he sent another similar list amounting to £188,000. The ground, he said in his letter, had been gone over so frequently between them that Mr. Bruce was well acquainted with his views. Being a local man, he knew exactly the standing of those who had now been made bankrupt. The letters had been found by the liquidator in the bank, and the jury would judge from them whether the Auditors were not fully conscious when they were arranging the Balance Sheets that they were not honest. It mattered not what influence was brought to bear upon them; their motives might even have been beneficent, or they might have thought their action would save the bank, but notwithstanding that, they would be quite as liable. No discretion was given them. Their duty was to tell the truth, regardless of consequences. The jury must remember that they were not trying the prisoners for the terrible results which had followed the reckless management of this concern. There was a

clear issue before them. Were the Balance Sheets false in material particulars? Did the prisoners know they were false, and did they sign and publish them with intent to deceive?

The following letters, which were written to the managers of the bank by the Auditors, were put in:—

“July 1899.

“Dear Mr. Shimmon,—As the time for the bank audit is approaching, we write to remind you of the promise you made us at our last attendance that various balances, to which we drew your attention, should be reduced. We hope you have been able to do this, or have obtained adequate security in respect to these overdrafts, as we are sure you will realise the difficulty of our position in signing the assets until these matters have been satisfactorily settled. Trusting to have your assurance that we shall not again be asked to pass these objectionably large balances,

“We remain, with kind regards, yours faithfully,

“WILLIAM ALDRED, SON & Co.”

“July 13 1899.

“Dear Mr. Shimmon,—In reference to your letter received yesterday, we note that you said it would be unwise to press some of your customers in regard to their overdrafts, as they might take offence and go elsewhere. But we submit that in several instances you would be in a better position if altogether relieved of such business, and that financially the bank would be stronger if these accounts were transferred to your rivals. We do not for a moment presume to dictate to you on a matter of management like this, but it will be apparent to you that each half-year we sign the account with more hesitation owing to what we consider the excessive overdrafts, in many cases the large amount overdrawn by your own directions, and owing to the fact that the security you should possess is largely pledged to English banks, as your own deposits are not sufficient to find the sums advanced by the bank. We are pleased to hear that you think you can satisfy us, but we hold very strong views on these points, and sooner than have any difference of opinion we would willingly retire altogether from the audit, although for so many years it has been a great pleasure to be associated with you.

“Yours faithfully,

“WILLIAM ALDRED, SON & Co.”

"Manchester, December 11 1899.

(Private.)

"Dear Mr. Shimmer,—In July last we wrote you as per annexed copy letter, and we now wish to draw your attention again to the same matter. As you will remember that on our attendance for the audit we considered that many of the balances were still most unsatisfactory, and it becomes increasingly difficult for us to sign accounts including so many increasing balances in respect of which we believe your security to be altogether inadequate, we must again press you most earnestly to make a determined effort to have them reduced, or to obtain satisfactory security, even if in some cases it results in the closing of an account, which, at all events, is preferable to eventually making a bad debt. Trusting you will understand our eagerness to have these matters settled,

"We remain, dear Sir, yours faithfully,

"WILLIAM ALDRED, SON & CO."

The witnesses for the prosecution having been examined,

Mr. Creer then rose to address the jury on behalf of Nelson and Rogers. He said their interests were separate. This was an important occasion to them, and he felt a grave responsibility. Both men he had known throughout his business life. With Nelson he had stood shoulder to shoulder at the Bar for 20 years, had seen him earn the respect and goodwill of his fellow-men from the beginning, until at last a few years ago he was within an ace of leaving the Bar and stepping on the Bench. If he had not been swallowed up in the whirlpool of speculation and greed which Bruce created—a whirlpool which swallowed up scores besides—Nelson would to-day have been a Judge in that Court instead of a prisoner at the bar. With respect to Rogers, he had for 20 or 30 years been the guiding spirit of one of the largest industrial concerns in the island (the Great Laxey Mines), and at the heels of the hunt had been grossly deceived by a man in whom he put his trust—a man who lied to his teeth from the first till the very last minute of their connection. That was the cause of Rogers being there that day. Counsel impressed upon the jury the importance of having a clear understanding of the questions they had to try. Negligence and carelessness were not sufficient. It must be clearly shown that they knew the Balance Sheets to be false, and that they sent them to the public with intent to deceive. Let them clear their minds of all cant about the smashing of the bank, and whether Nelson and Shimmer

took money. Another jury were about to try them on that charge; but now, if the 221st Section of the Criminal Code had not been violated, the prisoners must be acquitted. Counsel quoted on behalf of Nelson the ruling of the Judge who tried the Glasgow Bank directors in 1878, where it was laid down that, not means of knowledge only, but in point of fact that they did not know that the Balance Sheets were false alone constituted a criminal offence on the part of the Auditors. They were going to contend that the term "public officer" in the Criminal Code did not include Auditors, and that they, therefore, could not be tried for the offences imputed to them.

Deemster Shee said it was a pity the point was not taken before the trial.

Mr. Creer said he hoped this did not ruin his point.

Deemster Shee said he did not say it would; but he was disappointed that four advocates for the defence had not raised the question days ago, before the evidence was given.

Mr. Creer: I am sorry if I have made a mistake; but what I say is that public officials do not include Auditors. Had the Legislature intended to do so, there is no reason why it should not have included them by name.

Deemster Shee: Let us have your authorities.

Mr. Creer: There is no direct authority upon it. It was never discussed in England, for the reason that no barrister or lawyer has ever raised the question before. So far as I know, Auditors have never been prosecuted in England for issuing false Balance Sheets. The prosecution has always been for conspiracy.

Deemster Shee: Are you putting forward the point seriously?

Mr. Creer: Yes, your Honour; most seriously.

Mr. Hughes-Games: I don't raise this point for the other Auditors, your Honour.

Deemster Shee: You have considered it, I presume?

Mr. Hughes-Games: I won't say that.

Mr. Creer said they were acting quite independently. Dealing with the merits of the case, counsel said that the Auditors were deceived by Bruce, and induced to sign these Balance Sheets by representations he made to them. He admitted there were some foolish things done by them—some things which could not be called good accountancy. They

admitted that the £15,000 in notes were worthless, and the £65,000 loan was not properly included as cash in hand; but they had not then the full knowledge of the facts or anything to indicate suspicion. It must be proved that the notes were fraudulently included. Until Mr. Walker pointed it out to them, none of the officials thought there was anything wrong. As to the reserve fund, it was not contended that it was not properly sunk in the general assets of the company. Turning to the large overdrafts, the letters of the Auditors, said counsel, showed that they had suspicions, but no knowledge. When they inquired about them from the managers they were told lies, deceived, cajoled. Bruce told his chairman lies. Was it likely that he would stop at treachery to others? Bruce was in the midst of a maze of bankruptcies, putting off the evil day. No attempt was now made to justify the overdraft accounts; but their argument was that they did not know they were bad. The managers were in the heyday of their power, and to go to the directors for information would have been something like a farce. With respect to Mr. Nelson, he was only charged with issuing false Balance Sheets. He had produced statements showing him to be in a solvent condition. That statement had not been discredited, except with regard to the fuller's earth deposit, and if that £5,000 were struck out entirely, the statement of affairs would still have shown Nelson solvent. Nelson had every reason to believe, when he signed the Balance Sheets, that he would be able to meet his accounts. In a question of fraud, it was not a question of whether he was or was not solvent; but whether he believed himself solvent. There might be a fortune in the deposit of fuller's earth. Banks were in the habit of taking securities that the Government would not take, and it could not be said that that item should have been left out. Bruce, if he had had that matter in hand in his palmier days, would have made a sight of money out of it. There had been a lot of feeling against Mr. Mylrea, another director, with an overdraft, and it had even crept into the jury's notice; but if there had been any evidence against Mr. Mylrea he would have been in the dock too; but the Attorney-General very properly believed him innocent. What was the distinction between Nelson's and his account? If the coroner had gone into Nelson's house on the day he signed the Balance Sheet, every penny would have been paid, and if Mylrea had been forced to pay at that time the same course might have been resorted to. That was the only difference between them. The very nature of the transactions showed absence of fraud. They might have been merged in Nelson's General Account, and then the transactions would not have been so distinct against them. It would have been most difficult, if not impossible, to have formulated the charges, as the payments could not have been followed. There was no proof against Nelson that the

money had been paid for the Peruvian Corporation Account, except out of his own mouth. As far as Nelson was concerned, he was not aware until the close of the bank that the liability had been opened at Dumbell's. Bearing in mind that Nelson had claims against Bruce, could the jury say that in June 1898 he was aware that he would not be in a position to pay the amounts due by him? It was said that on the face of the accounts it was apparent they were not good debts. The reply was that Mr. Nelson had shown that at the date he signed the Balance Sheets he had believed himself solvent.

The Attorney-General having replied to the argument that Auditors were not public officers under the Manx Statute,

Deemster Shee said: I have no doubt about it; in my mind, in any public company which is registered and incorporated, the Auditor is unquestionably a public officer.

Mr. Coole said it now devolved upon him to rebut the terrible charge of deceit and swindling brought against Mr. Shimmon. His honour was his life, and if they stamped him as a criminal, what was there to live for? The high character he had borne was too well known to bring evidence in its favour. Since the bank closed on that doleful day, the 3rd of February, there had been one continuous cry for vengeance upon the managers of the bank. Money had been lost, people had suffered, and in every household in the island every man, woman, and child had tried the prisoners at the bar, and he supposed in the majority of cases condemned them. The jury must have talked of the thing a hundred times, but counsel appealed to them to put from their minds the clamour for vengeance and judge the prisoners strictly according to law and to the evidence. He admitted that Mr. Shimmon did not make so good a witness as the others; but this was the result of the severe mental anguish which he suffered under the skilful cross-examination of the Attorney-General. The essence of this crime, however, was guilty knowledge and corrupt motives. Had these been proved? Mismanagement and loss of money was not enough to prove it. God knew that loss had been felt heavily enough all over the island, and no one felt it more than Shimmon and the other prisoners. There had been great carelessness, but wicked, misleading intentions there were none. Shimmon had implicit confidence in Bruce, and Bruce had deceived him in the same manner as the others. It cut him (counsel) to the heart to say such a thing, but the evidence given showed that Bruce was an arch deceiver, who deceived his directors, who deceived his under-manager, and who deceived the Auditors. The death of Mr. Bruce was an unfortunate circumstance

for them, for it was now argued that they were trying to shield themselves behind him. Would to God that Mr. Bruce were alive to-day, that he might come forward to exculpate the prisoners in the dock, as counsel was sure he would have done. Bruce would have confessed that he, by lying and falsification, had deceived them. The jury must be convinced that Shimmon, in making these Balance Sheets, not only knew they were false and fraudulent, but that he succeeded in deceiving the public. It was said that the fact of Shimmon protesting showed his guilt. On the contrary, it proved his innocence. He was on the horns of a dilemma. If he protested, it was to be taken as evidence of guilt. If he had not protested, it would have been said that he stood by without asking a question, and allowed the shareholders' money to be squandered. Another point which would be made a good deal of was that Shimmon received £700 a year. Was a man's criminality, then, to be measured by his stipend? It was perfectly clear that Shimmon was Bruce's subordinate. Bruce was strong-willed, high-handed, and rode rough-shod over his colleague. With the branch accounts Shimmon had nothing to do, and as to the large overdrafts to Douglas tradesmen, he had every reason to believe that the contingent fund and the reserve fund, amounting in the aggregate to £84,000, would meet them if bad, although he was satisfied by Bruce that they were good. What reason had Shimmon to think that Bruce, the king of finance, as he was known, had made a mistake in making up these accounts? As for the securities, gilt-edged securities in unimpeachable concerns had depreciated 50 per cent. What prophet would have foreseen two years ago a calamity which had ruined prisoners and ruined these accounts? It was Shimmon's misfortune that all his actions in the interests of the bank were misconstrued. Coming to Shimmon's liability on the Peruvian Corporation bonds, counsel submitted that the evidence did not show that his client participated.

The Attorney-General said he did not press that against Shimmon.

Deemster Shee pointed out, however, that Shimmon drew up the debit slips by which the money was taken from the bank.

Mr. Coole: It is not now contended that Shimmon benefited from that transaction.

Deemster Shee: No; everybody lost, the bank as well. (Laughter.)

Mr. Coole said it had been the subject of second indictment against Shimmon that he had misappropriated the money drawn for the Peruvian speculations; but that was now withdrawn. The Nelson Loan Account was opened temporarily by Bruce in Shimmon's name,

and afterwards Shimmon pressed Bruce to free him from the liability, and the cheque on Nelson's Loan Account was drawn to pay the debt standing in Shimmon's name. Shimmon was then aware of the overdraft, but he always understood that good, solvent men were liable for them. Mr. Shimmon entered with Mr. Bruce into the speculation in Allsopps to the extent of 30 shares, and had then told Bruce he would go no further. There had not been a word of evidence that Mr. Shimmon was not able to pay any liability in connection with Allsopps. It had been said that it was no crime to take money if it could be repaid, and they had an object lesson in this in Mr. Mylrea not being here. There had not been charged a single falsification in the accounts. Every entry in the books was correct, and if the amount that had been put down was not realisable it was but an error of judgment. Reverting to the £65,000, Mr. Coole said that fabrication came originally from Mr. Bruce. The Auditors had asked Shimmon, and he told them what he knew, and Bruce when brought up also stated that it was a loan to the Tramway Company and not to the bank, as was the actual fact. Mr. Shimmon had no knowledge that would bring him within the charge of deceiving. Proceeding, counsel said he was not going to defend the inclusion of the notes; but denied that it was done by Shimmon with intent to swindle. He was taught the practice by one of the most honourable and business-like men in the island, George W. Dumbell. He left his client in the hands of the jury. It had not been shown that Shimmon had one cent to gain by this terrible fraud. Did they believe that this person of unblemished character, who had walked about Douglas for 60 years, who had been everywhere respected for his honesty and integrity, had intended all along to rob the people of the Isle of Man? He believed they would say, and he longed to hear the words from the foreman, "Not guilty." Shimmon was not a robber and a rogue. On the contrary, the evidence showed he was an honest, upright, straightforward man. He (Mr. Coole) asked the jury to restore him, broken-hearted and broken in spirit, to his sorrowing ones at home, where, with this fearful charge, this nightmare, taken off him, he would enjoy some of that rest which he spoke of in the box, and for which his weary soul yearned. Counsel left the remainder of his life in the hands of the jury, and did it with confidence.

Mr. Hughes-Games, addressing the jury on behalf of the Aldreds, said Deemster Shee had asked why expert evidence had not been brought forward to show that the Auditors had properly performed their duties, and the reply was that no accountant could have been got who would say that the Auditors had not done their duties as they should. An accountant who undertook to say otherwise would have

sacrificed his own reputation. Reviewing the evidence as to the duties which H. V. Aldred exercised in the audit, counsel reminded the jury that he merely checked the additions and did other clerical work. On one occasion he had written the certificate for his father and partner to sign. Civilly, he might be liable for the acts of his father, but not criminally.

The Attorney-General said he contended that Aldred, junior, consented to the issuing of the Balance Sheets.

Mr. Hughes-Games replied that Harold was only a partner in name, and Mr. William Aldred was the real Auditor of the bank. He (counsel) would not attempt to justify his method of auditing. He would put forward merely that he was an old man, a confiding old man; that he fell into the hands of men who duped and deceived him when he honestly trusted and confided in them. As to the unissued notes, it was a mere error of judgment. The notes had been so treated from the formation of the bank, and Mr. Aldred had continued a practice which he now admitted was wrong. He was an old man, and it was the mistake of an old man who was not now in the full enjoyment of his mental vigour and was without any guilty intention. As to the £65,000, that appeared in the Ledger, "To Cash, £65,000." He did not wish to suggest by whom that entry was perpetrated, and he would not dispute that it was placed there to improperly swell the cash in hand. It was put there for the purposes of fraud, but Mr. Aldred did not detect that fraud standing by itself. The entry showed cash at the London City and Midland Bank of £65,000 to the credit of Dumbell's Bank. It appeared so in three half-years. It was true, and he did not wish to blink the fact that if it was liable to arouse suspicion in the first half-year, it was more liable to arouse suspicion in the second and third half-year. No interest was ever charged upon it, and it was considered impossible by the prosecution that business men should ever pass that entry without detecting it as a fraud. The managers then would be known as criminals and frauds to every clerk in the bank. No; it was not so patent as all that. There was mystery about it, and as even the head cashier in the box admitted, it was difficult to understand. Mr. Walker, the liquidator, said he would have asked for a voucher from the London bank. No doubt that was a correct thing to do by a thoroughly conscientious, competent Auditor. Mr. Aldred did not do it, and that was the sole explanation. He was not likely to come to the conclusion that gentlemen with whom he had been in closest contact for so long were dishonourable and guilty of piracy. It was not suggested that the amount was correctly treated. All that counsel suggested was that Mr. William Aldred honestly believed it was right,

and that he was a silly old man. With regard to the overdrafts, an Auditor had to be very sure of his facts before he interfered with the management of a bank. Mr. Aldred was a stranger coming twice a year to the island, and staying five days. He had no local knowledge, and had to rely only on the material found at the bank. The manner in which he conducted the audit was, again, incomplete. He merely looked at the totals of the certified branch returns and the Douglas accounts as they stood in the Ledgers. He never looked through the details, and only seldom compared the increasing balances with the previous half-year. When the managers were questioned, he received assurances that the accounts were all right, or if there was some slight loss it would be fully covered by the contingent fund. The managers also allayed his fears by increasing the contingent fund, and setting aside in three half-years £12,000. The question was asked why the Auditors sent their first letter in 1885 to the directors and subsequent letters to Mr. Shimmon. Counsel suggested that the true reason was that in the first instance one of the managers had guaranteed certain overdrafts, and they wanted to be certain whether he was good, but in the later letters they wrote as a matter of course to Shimmon as the secretary.

Deemster Shee asked in whose handwriting the letters were.

Mr. Hughes-Games replied that that dated 11th July 1899 was written by Harold and signed by William Aldred for the firm, and contained a copy of a letter sent on 7th July. These letters, continued counsel, were the most important evidence for the prosecution; but if William Aldred knew that the advances were bad he must have known the managers knew. His letters were transparently honest, for he innocently suggested to them that these accounts should be transferred to Dumbell's rivals. He did not care to interfere with the policy of the management, and rather than dictate would willingly retire from the audit. The letters denoted strong distrust and discomfort, but not knowledge. The jury might think they established a state of mind which amounted to knowledge; but they must remember that unless Aldred knew there were false statements, it was not his bounden duty to do anything rash. If he had resigned his position the result might have been disastrous. It was only when he became aware of the facts that he could ask to be allowed to resign. He stood between the devil and the deep sea, but unfortunately he had not the necessary knowledge to enable him to take the necessary plunge, and he was now landed in the arms of the enemy of mankind. Without disrespect to the prosecution, he (Mr. Hughes-Games) was quite sure the jury would find it their Christian duty to release him from his toils. What inducement, he asked, could William Aldred have for signing the

Balance Sheets? Nothing appeared in the letters. He evidently did not even know, like Rogers, that the bank was going to be sold. There was absolutely no inducement. Much, no doubt, would be made of the wording of their certificates, that they had made a full examination of the books and certified branch returns. They had not and could not possibly have made a full examination, and counsel contended that while that might make them liable civilly, it did not amount to concurring in issuing false Balance Sheets. He came now to the most painful part of his address—namely, to point out matters which must have a telling effect against their co-Auditor Rogers. Evidence had been given that he was warned of the state of certain accounts, and he was a local man with local knowledge; they had a right to expect from him support, loyalty, and co-operation, instead of which, the evening before the audit in June 1899, Rogers wrote to Bruce, prepared him to meet the points that would be raised, and thus joined in a combination against his co-Auditors. Considering all these things, and that William Aldred was a stranger in a strange land, it was not exceptional that he should have been deceived. Twenty years ago he was the Auditor of the Manchester Savings Bank, but his faculties were not now what they had been, and while he was no doubt a good calculator and a man of figures, he had not the discretion nor the ability to grapple with the audit of this bank. All William Aldred's accounts proved that he was innocent. At the suspension of the bank he had over £300 there on deposit, a sum considerably more than three years' fees. That his fees could have been any motive for him signing the certificate was too paltry to refer to. Counsel put it to the jury that William Aldred was an old man without judgment and easily deceived; that, like the other directors who had received a fool's pardon, he had simply neglected his duty, and, like them, was entitled to pardon. Upon the jury lay the heavy responsibility of saying whether, in the absence of motive, this old man signed those Balance Sheets with a full knowledge that they were false—or whether, confiding in the truthfulness of others, he believed them true. Whether he left the dock as a free man or a convict, he would go forth to the world with the knowledge that his professional work was done, and with the prospect before him of being rendered destitute by an enormous civil liability. With sorrow he must feel to the end of his days that what he had left undone had caused so much ruin and suffering in that island.

The Attorney-General rose to reply. He asked whether the Balance Sheets were not now admitted to be false? If they were false in any material particular to the knowledge of any of the defendants that was enough. There could be no question as to the materiality of certain items, more especially the notes, the £65,000 loan, the advances to

customers which included bad overdrafts, the so-called reserve fund, and the amount of profit and loss. Let them first consider the position of each defendant, and it had been said they were suffering by the death of Mr. Bruce. Why, the very absence of Bruce, his inability to contradict their statements, to remove the heavy burden of guilt which they had thrust upon him, was of the greatest possible advantage to the prisoners. No one had gained more from the death of another. Shimmon's position could not be reconciled with that of a counter clerk. To him all the clerks went for instructions. With him the Auditors discussed the overdrawn accounts. He alone was often closeted with Bruce, talking over the management of the bank. The theory that he was a clerk could not be accepted. The opportunities he had of knowing the facts must be considered. With regard to Nelson, it was probably as true of him as of the other directors that he did not know of the way the notes and the £65,000 loan were treated on the Balance Sheets, but his own accounts must have given him criminal knowledge. The duty of the Auditors was to test every figure in the books. To the contention that Harold Aldred was not one of the partners, the Attorney-General asked, Did he not attend the audit? Did he not write those letters? Did not his name go forth as one of the firm? It was idle for him to say he was not responsible, because he saw the Balance Sheets every half-year and allowed them to go forth to the world. It was of the greatest importance that the bank should have plenty of cash in hand; yet $12\frac{1}{2}$ per cent. of the total at Dumbell's was represented by the notes. The £65,000 loan made another 64 per cent., leaving only £34,000 cash actually in hand to meet deposits of £1,299,170. The Attorney-General contended that Shimmon's allegations with respect to the £65,000 loan were too strong, and disproved what he said. This so-called loan was never used, never operated upon, and never drawn upon in any way. There were also the monthly statements coming to Dumbell's from the London City and Midland Bank, and here the item was debited against them. If it was to the Tramway Company, as Shimmon said, why was it not sent direct? Did those monthly statements say the interest was a charge for the Tramway Company? Nothing of the sort. Again, the tramway debentures were not issued till some months afterwards. This pointed irresistibly to a direct loan to Dumbell's, and was further strengthened by the letter which the general manager of the Midland Bank wrote to Shimmon on 11th October 1899, showing the exact position of affairs between the two banks. Could the jury after that evidence believe Shimmon's story was true? If they did, let them give him the benefit of the doubt. He (Mr. Ring) was not the man to press a case unfairly against a prisoner. Thank God, he said, he was not the

judge of these facts; but the jury were. He pointed out that Shimmon must also have been cognisant of the loan being to Dumbell's from the letters sent to Bruce from the Midland Bank. How could the latter threaten to stop Dumbell's cheques if they had £65,000 lying with him?

Mr. Coole said no letter ever came into Mr. Shimmon's hands.

The Attorney-General replied that this was the first time he had heard that contention. He could put in other letters showing that he did receive the document addressed to him dealing with the letter of the Aldreds on the 13th of July 1899. Counsel drew attention to the remark that the securities were largely pledged to English banks, and asked whether they could really have thought of using such language that there was £65,000 cash in hand. They were told by William Aldred's counsel that he was a silly old man, and an appeal was made for his acquittal on that account. No one could be so devoid of feeling as not to pity the prisoners in their present condition; but considerations like that were foreign to the inquiry, and the jury must deal with the matter as business men and as men of the world. He protested against the acceptance of the theory that William Aldred was so incapable and stupid as to be irresponsible for his acts. The overdrafts went up at the rate of £100,000 in the half-year. A school-boy could have understood the figures. Dealing with him in the spirit of the largest charity, could the jury come to the conclusion that he was ignorant of the effect of the figures? Rogers, the other Auditor, defended this condition of things up to the last, but brought no one forward to support him. Could it possibly have been the state of his mind that he believed the £65,000 was cash in hand? Counsel asked the jury to consider well whether this item must not have been staring the Auditors in the face aggressively? The contingent fund and reserve fund were merged in the general assets, instead of writing off the bad debts, which not only put a fictitious value on the assets, but swelled the profits of the company. It was undisputed that the assets were over-stated on each Balance Sheet £150,000. No knowledge had been brought home to Nelson that he intermeddled in the interior working of the bank, but Shimmon was frequently consulted when these overdraft customers came in. What was his excuse for his conduct in the matter? Merely, "Bruce told me they were good." Counsel admitted Mr. Bruce was indeed a wondrous personality, and had a marvellous charm of manner, but no moral terror nor strength of will was any excuse for an offence if that led him into a crime. It was a consideration for the Judges, but not for the jury. Shimmon's fault was that he did not protest enough and place himself above reproach. He quite disagreed with the defence that a bank Auditor could not test

the stability of customers; on the contrary, a bank Auditor was most happily situated. Had they the books at all before them, they must have known these accounts were not good, and be guilty of flagrant breach of the law. Rogers, again, just before the last Balance Sheets, submitted a list to Bruce containing doubtful debts to the extent of £127,675. The Aldreds about the same time—December 1898—wrote hoping they would not again be asked to pass these objectionably large balances. This letter was addressed to Shimmon personally, and was in the handwriting of Harold Aldred. There was knowledge brought home to Aldred, junior. It was seriously suggested that one of the proofs of old Mr. Aldred's innocence was that he recommended Shimmon to transfer the bad accounts to their rivals. Why, they were not marketable, and could not be transferred had Shimmon wanted to, which he did not, for he was afraid of losing customers and so reducing the bank's fictitious profits. Was it compatible with the theory that Mr. Aldred was not concerned in the state of things that he wrote saying the security was altogether inadequate, and rendered it increasingly difficult for them to sign the accounts? Rogers' private and independent letter to Bruce at this time was a remarkable communication, and showed clearly that he had knowledge. The certificate they procured from the managers at every audit only tended to strengthen the evidence against them. The relief in the accounts that they asked for in December 1898 had, six months later, far from being given, gone worse to the extent of £38,000. Had the Auditors dropped one little private note to the directors, they might have saved themselves from their present position. The jury would draw their own conclusions from such conduct, and say whether Mr. Aldred deserved a fool's pardon. All the misgivings he ever entertained were crushed out as half-year after half-year he put his name to the Balance Sheet. The jury had nothing to do with the motive. The very fact of Mr. Aldred having a deposit at the bank might have been one of his motives for tiding over their difficulties. The law was clear; the Auditors must tell the truth irrespective of consequences, and the only question the jury had to weigh was not the motive, but did they know? Coming to Nelson's accounts, the jury would see that his remarks bore also on the address, because these accounts would naturally excite suspicion. There was a wide distinction between Nelson and the other defendants. There was first Nelson's General Account at Ramsey. Although the Auditors did not audit the branch accounts, it was admitted that they knew of their existence from June 1896 to December 1898. This General Account of Nelson's sprung from £7,800 to £29,620. Nelson said a large part of this was interest, but that was irrelevant. The charge was putting them forward as good accounts. Then, in regard to the

Nelson Loan Account for £5,822, Shimon said this was a temporary loan to Bruce till he received a cheque for £5,000 from Liverpool, but the manipulation of the account did not bear out his statement. What information they had of this account was derived from Nelson, who openly admitted that he was jointly liable with Bruce and Shimon. Respecting the triple account for Peruvian bonds, £8,000, Nelson now denied liability, and the jury would have to say whether, being up to his neck in speculative accounts of this nature, he had any particular reason for wriggling out of this. Here, again, Shimon made out the slips by which the money was taken out of the bank; but as he denied personal liability, counsel did not press this against him. But turning to the far more serious matter of the speculations in Allsopp's shares by which, between April and December 1892, £22,600 was drawn out of the bank, the jury would see that the account was kept at Ramsey. They would have to consider if there was any motive in this. Shimon, though he made out most of the cheques, and the shares stood in his name and that of Bruce and Nelson, denied liability, and said the speculations were on behalf of the bank. The shares were not in the bank's Securities Book. Shimon knew this, so that it was hardly likely the speculations were for the bank. How did they draw on the bank's funds to pay for them? They drew on the Nelson Trust Account, and Nelson took credit in his statement of affairs for Shimon being jointly liable. Nelson's evidence with regard to Shimon's position was, it was only fair to say, exceedingly weak. Nelson had made out certain Balance Sheets to show that he was solvent; but the question now was not misappropriation, but did he sign Dumbell's Balance Sheets knowing them to be false? Moreover, his assets were based on being nursed and properly realised. These, however, were not considerations for that jury. The question was: Did he believe the assets were good, or did he know they were rotten? There had been the grossest neglect, a shameful breach of duty by all the directors; but Nelson differed from them in this, that he was acting with others who had knowledge of the state of things. Concluding his address, the Attorney-General said he trusted he had put the case before the jury in a way which would enable them to bring to bear a perfectly impartial judgment. That was all he asked for. It had been said that a cry for vengeance had gone out from the public of that island. If that were so, to none was it more abhorrent than to himself, and no one would more gladly join in the condemnation of that and all other outside attempts to interfere with the upright and impartial administration of justice in that Court. No, let popular passion if it liked beat in vain against the walls of that Court, the calm atmosphere of that tribunal it could not disturb. It had no place there that day, and the jury would

disregard it. Let the still, small voice of conscience speak to every heart in that box, and if, led by that divine guidance, they made their final pronouncement upon the issue, big with fate, as no doubt they would, he was satisfied that, whether their verdict be in condemnation or exoneration of the prisoners, the verdict would commend itself to the best, the purest, and the noblest opinion of their fellow-countrymen.

Deemster Shee, in charging the jury, said there could be no doubt that this case was of the very greatest importance to the community and important in its consequences to the defendants. He should not be using too strong language in saying that a miscarriage of justice in this case would be a misfortune to everyone in the island. If the defendants were acquitted out of sympathy, that would be a miscarriage of justice; and if they were convicted out of prejudice, that also would be a great miscarriage of justice. Every care had been taken to obtain an unbiassed jury. The right of challenge had been freely exercised. The jury in the box had been put there and sworn to try the case according to the evidence. He believed they would do their duty, and do it according to the evidence they had heard in that Court. In substance the charge came to this: That the defendants had all had a hand in making and circulating Balance Sheets that were false in several particulars—though one would be enough—Balance Sheets which they issued intending to defraud. There was no dispute, except by Harold Aldred, that all of them did issue the Balance Sheet. Shimmon took a leading part in compiling them, and all the Auditors took part in auditing the accounts. The signature of one of them was enough. It was equally clear that the Balance Sheets were false. It was not now denied that the £15,000 unissued notes were wrongly stated as cash. Then, with regard to the £65,000 loan, the fact was that no cash passed from the London bank to Dumbell's bank. The fact was that it was described as a loan with a corresponding allegation, the accounts showing a much larger balance owing to the London bank. Dumbell's, in the first half-year, owed £89,000, in the second half £101,000, and in the third £180,000, and yet it was treated as cash by the managers and Auditors, and was treated as cash in the Balance Sheets, which should represent the true state of the bank's affairs. Whatever might be the opinion of other people, the jury, using their best intelligence, would probably see that this £65,000 was as little cash as the £15,000 notes. As to overdrafts, those which were good were all right, but it was with regard to bad overdrafts that the jury had to apply their mind. Let them distinguish between the two sorts. Beyond all question, these overdrafts were bad, he (Deemster Shee) should say; but the jury must not accept his opinions, but form their own. He believed they were hopelessly irrecoverable. In June 1898

there were £234,000 of this class of overdrafts; in December 1898 there were £243,000; and in June 1899 there were £281,000 worth of them. Not only that, but there was £30,000 of overdrafts included which were confessedly and hopelessly dead. No interest had been charged on these since 1884 and 1885. He accepted the view of the prosecution that, though the overdrafts did not tell against Nelson, they did tell very strongly against the manager and the three Auditors who had the fingering of these books. Every half-year there was a regular, heavy decline shown, and the jury could not refuse to accept the Attorney-General's statement that while the manager and Auditors were experts at accounts it needed no expert person to tell that they were hopelessly and irrecoverably bad. Some of the overdrafts were statute-barred four times over, but all were treated as assets and interest charged upon them. Here, again, the Balance Sheet was false. It was not denied that the accounts were false, and that the bad debts over-topped the reserve and contingency fund combined over £100,000. Besides this there was £6,000 interest improperly added. It was uncontradicted evidence that if the cash had been properly shown at £35,000 instead of £120,000 everybody with a penny at the bank would have run to withdraw the deposit. There was no question, then, that the accounts were not only false, but materially false. The real question was: Did any or all the defendants know they were false? Whatever they might do in their own business, the law said managers and Auditors of public companies must tell the actual facts, whatever they might be. If they knew the overdrafts were false, there was no doubt what the duty of the jury was, and they must do it in spite of everyone. First, with regard to Nelson, a good deal had been said about the duty of directors. It was asked why the other directors were not there. The jury had nothing to do with them; "sufficient to the day was the evil thereof." The jury had quite enough to do, and ought to thank God Almighty that they had five and not eight officials to try. From what he (the learned Judge) had heard, the other directors were not criminally liable. On the contrary, it seemed to him Mr. Mylrea's overdraft was a very good account to the bank. The question was, did Nelson know the Balance Sheets were false? He was not bound to be suspicious, and was not liable if he signed the Balance Sheets in ignorance of the facts. On the other hand, he was not a dummy director. He was an educated man, an advocate, and a solicitor, and a man of business not likely to go wrong through carelessness. It had not been contended nor proved that he knew of the inclusion of the £15,000 notes and the £65,000 loan; but the overdrafts were another matter. His own were so heavy that the jury could hardly suppose he could ever have forgotten them. He must have carried the knowledge of them through

all his occupations, let alone when he signed Balance Sheets. His overdraft in June 1898, including the various loans, was £62,800, and in December, the same year, it was £63,800. What was his defence? He said he was a man in a large way, that when his co-obligators had paid their shares he owed only £42,000, and had assets valued at £54,000 to meet it; but he had told his trustee in bankruptcy that his assets were worth only £30,000, and he could not possibly have estimated his assets like this when he signed the Balance Sheets in 1898. The estimate was only made at the pinch of the man's life. He naturally gave his assets their fullest value. People did not over-rate their own properties, and even expert valuers differed widely. The Attorney-General, who had been conspicuously impartial, asked whether the fuller's earth deposit would have been taken as security by a London bank for £5,000? If Nelson believed his accounts good when he signed the Balance Sheets, then the prosecution failed; but the jury must remember he was a director and advocate, a shrewd man of business, and not likely to go wrong in error, and this was not the only indirect evidence against Nelson. The triple accounts opened in his name, and amounting to £34,800, were, it was important to remember, losses alone. It was conceded that neither Nelson nor Shimmon found the money. They only said they believed Bruce found it. Did they know it was the bank's money? If they did they knew that the directors' consent had not been obtained, and that it was just as much like taking money out of the tills as if it was spent on the turf. There was direct evidence by Nelson's own admission, he joined Bruce in the Peruvian speculation; but the indirect evidence was stronger still. Because, could the jury think that he believed that Bruce could get, and did get, the money to pay for these bonds just for asking a London banker? Nelson knew the money was not Bruce's, or it was not Shimmon's, and he must have had a strong impression it came from the bank. The story Nelson told might be a pure fiction. It was for the jury to say whether it was credible. Shimmon said the only deal he ever had was in 30 Allsopp's shares, and that he only consented to act as Bruce's nominee because Bruce did not want his name appearing on Allsopp's books. Why had he any hesitation, if it was an honest transaction? He swore he believed it was for the bank, but he added, "I did not like it; I thought it was too speculative, and ought to go before the board." The securities, however, never got into the bank's Securities Book, although he knew it was the bank's money that was being used. They had to discover the truth if it had not been told. The Nelson Trust Account opened at Ramsey was originally Shimmon's No. 3 Account at Douglas. How did he come to allow it to be opened in his name? He admitted that he did not like to be mixed up in it;

but if it was all right, what was the harm? A large sum went to Liverpool and never came back; another thousand went to Nelson, all out of the bank, and then Shimmon got tired of it, and asked to be relieved. But the jury must not only hear what the defendants said, they must read between the lines, and come to an honest and fearless conclusion. As to the Peruvians, Shimmon made no bones about it whatever, that he made out the debit slips by which the money went out of the bank. He got tired of the accounts standing in his name, and Nelson said, "Oh, never mind; put them in my name." There they had two most obliging friends. (Laughter.) The accounts were transferred to Ramsey, where there was no audit. There were no distinctions in a Court of justice. The educated and uneducated directors, managers, and Auditors must be tried with the same care and as fairly and fearlessly as each other. It was Shimmon's business, as manager, to deal with details, his business to superintend the preparing of the Balance Sheet. All of them had found fault with one who was dead; but he (his Honour) did not want to say any more about him than he could help. Did it never occur to Shimmon that it was wrong to treat the unissued notes as cash? He also instructed how the £65,000 loan was to be entered. It lay there year after year without any transactions upon it. Let the jury remember how essential it was that a bank should have plenty of cash in hand, and then consider if Shimmon and the Auditors could really have thought these two items were cash. Respecting Shimmon's position in regard to the overdrafts, it was not denied that ten years ago his attention had been called to these particular accounts. He had them under his nose constantly from various sources. The clerks and the Auditors, who necessarily had the details before them, called Shimmon's attention to them. He said he protested to Bruce, but allowed cheques for a large amount to pass. Why did he not protest to the directors? His protests had as little effect as a wave upon a rock. Then who destroyed the Overdraft Book? Did Bruce? So much had been said against that poor man that his Honour did not want to say anything more; but let them conclude that Bruce destroyed it. There was no Securities Book. Shimmon had asked to see it, but he did not see it. Was he speaking the truth? He accepted Bruce's assurances. Considering the number of unbelievers there were in the world, it was astonishing to find what a number of believers in Bruce there were. Did the jury believe, as business men, that a bank manager and an Auditor of the city of Manchester would take the assurance of anybody when their suspicions were aroused? Without giving any offence whatever, they would ask to see the securities. Whatever Shimmon attempted to make out in the box, he was in no sense a man behind the counter. He was, according to

Nelson, a co-speculator ; according to his own statements, he discussed the accounts, and, what was more, he signed the accounts. He was a man in a sufficiently independent position to have brought those important matters, on which his suspicion was aroused, before the directors. Were the jury satisfied that in any one of these particulars he had called attention? Did Shimmon know of the rottenness of the account? If the jury so believed, Shimmon was guilty of circulating a false Balance Sheet. The three Auditors' case remained. First of all, an Auditor represented the shareholders, and was there to protect them. His business was to exercise an independent judgment. He was not to take the directors' nor the managers' view ; but, if suspicious, must probe it. Auditors were not to be mere arithmeticians and calculators, as, it was said, Aldred, junior, was. Their duties were clearly laid down in the ninth article, and the defendants must have known it, for they professed to have gone very fully into the accounts. They must make an audit certifying the true state of affairs at the time of the Balance Sheet, and, though not liable for carelessness, they must be honest and tell the truth. All the defendants might be treated as one. All of them received the same assurance. If they did not, it was difficult to see how they agreed as to the notes, the loan, and the overdrafts, and all the other items on the Balance Sheets. It must have been apparent to them that cash in hand was an essential feature with the Balance Sheet, and that the £80,000 to make the bank look strong had to be got somehow. It was conceded by them that the notes and loan were not in cash. Their letters showed that they unquestionably thought the overdrafts were bad. The written assurances they obtained from the managers proved that they thought the accounts were so bad that no one would believe that such assurances were given unless produced in writing. The Aldreds told the managers they held strong views on the overdrafts ; but did not certify those strong views on their certificates. Did the jury think that, covering so many years, they were convinced by Shimmon's and Bruce's assurances, or did the jury believe they were unconvinced? Still, did they tell the shareholders that they had had differences with the managers? No ; they said, "We have examined the accounts in detail and find them to be correct." Did they examine the accounts in detail? Let the jury assume they did. Did they then find them correct? They also certified that they had examined and satisfied themselves that the securities were satisfactory and in order. Were the Allsopp's and other securities in order? Notwithstanding what they wrote, the evidence was that they meant the reverse. Did the jury mean black when they said white? No ; the object of a false Balance Sheet was to keep the company going. It was said on the one hand that Aldred, senior, was too old, and, on the

other hand, the other was too young. There was not a middle-aged partner in the firm. Age had nothing to do with it. Aldred, senior, knew what was going on. If the jury thought he was a mere machine, it was their duty to say so; but if they thought he was a man of intelligence and grown to years of discretion, and knew these things, there was no doubt he was guilty, and the jury must say so. There was little difference in regard to Rogers. He joined in some of the letters with Aldred, and wrote another to Bruce on his own account, which, Aldred said, was to put Bruce on his guard. There was another question: Whose was the motive? Why should the Auditors do this? Why should they say a thing was true they believed to be false? The jury had been a long time inquiring into the case, and they would be taking a great deal on themselves if they inquired as to the motives of the various parties. All the motives in the world would not make a dishonest thing honest. Let them not be diverted from the main issue by inquiring as to motives. Character had been properly referred to. When a man was in need, as he was when in the dock, it was right that he should have the assistance of his friends. As to their opinion of him, all the people concerned might have been honest and upright, except perhaps unfortunate Mr. Bruce, but what had character to do with the offence? We could not make good bad; we were all honest until we were found out. If there was a doubt, they should give the prisoners the benefit of it. The case had been well conducted on both sides, and he himself had endeavoured to summarise the evidence on both sides for the purpose of endeavouring to assist them. It remained for the jury to do their duty as firmly, as fairly, as conscientiously, and as truly as everybody else in the case had endeavoured to do. He now dismissed them with these remarks to the consideration of the case, and expressed the hope that they would arrive at such a decision that the public of the island would be perfectly satisfied that the verdict they had given was a verdict according to truth and justice and the oath they had taken.

The jury then retired, and after an absence of 70 minutes they returned into Court.

Deemster Moore asked if they were agreed upon their verdict.

The Foreman: We are. We find all the defendants guilty, Harold V. Aldred in a minor degree.

Deemster Shee (to the foreman): Do you mean he is guilty, but you recommend him to mercy?

The Foreman: Yes; that is what we mean by the expression.

C C C

Mr. Hughes-Games asked if it was the intention of the Court to pass sentence before hearing the other charge. If so, he wished to address the Bench in mitigation of the sentence on the two Aldreds.

Deemster Shee, after consulting the Governor and Deemster Moore, said they had decided to defer the sentence till after the other case was disposed of.

The prisoners were subsequently sentenced: Nelson and Shimmon to five years' penal servitude; Rogers, eighteen months' imprisonment with hard labour; William Aldred and Harold V. Aldred to twelve and six months' hard labour respectively.

(Condensed from *Acct. L.R.*, 1900, p. 181.)

The case of **FOSTER v. THE NEW TRINIDAD LAKE ASPHALTE CO., LIM.**

(Decided before Mr. Justice BYRNE, in the Chancery Division, on 28th November 1900.)

Held that an unexpected appreciation in the value of Assets taken over by a Company at its formation is not Profit available for Dividend, even though the Asset in question be a Book Debt.

This application raised an interesting question of company law as to the proper method of dealing with an unexpected appreciation of assets. The facts and the nature of the arguments are sufficiently stated in the judgment.

JUDGMENT.

Byrne, J., said: This is a motion on behalf of debenture-holders and of a shareholder in the defendant company to restrain the application in or towards payment of a dividend of the principal of a certain debt recently paid to the defendant company by another company called the New York and Bermudez Company. I treat this as a motion on behalf of a shareholder seeking to restrain an *ultra vires* payment. In the year 1894, an American company (referred to in the affidavits as the old Trinidad Asphalte Company) acquired the stock and bonds of the New York and Bermudez Company, and also a debt

of \$100,000, due from the latter company, secured by promissory notes. In 1897 the defendant company, which is an English company, purchased the property and assets of the old Trinidad Asphalte Company, including the debt due from the New York and Bermudez Company, and on December 31 1899 the New York and Bermudez Company gave to the defendant company new promissory notes for \$127,000, being the amount of the debt of \$100,000 with accrued interest then due. This \$127,000 has recently been paid off, and the defendant company, through their directors, are proposing, without reference to the other business or assets of the defendant company, to treat the whole of that sum, amounting to £26,258 16s. in English currency, as assets available for dividend, and to distribute the same accordingly. This is the statement in the plaintiff's affidavit, and it is not denied by the defendants, so that, although some discussion took place in argument upon the point, I have not now to consider whether or not the amount in question may properly be brought into the next Profit and Loss Account, but simply whether or not the amount may be divided as profit with regard to the present value of the total capital assets, and whatever the result of the year's trading may be. No question is raised as to so much of the sum as represents interest, the point at issue being as to the amount representing principal of the debt. There is no doubt that the debt formed part of the assets originally purchased by the defendant company, and as such part of its original capital assets, but it is argued that as the debt was not regarded or treated as an asset of any value upon the purchase, and as it has not appeared in the former Balance Sheet as part of the assets of the company, and as the only entry in relation to it in the books of the company is a Journal entry carrying the notes to a Profit and Loss Account, it ought to be regarded as a windfall in the nature of an unexpected profit, and as divisible accordingly amongst the shareholders. I cannot accept this view. Although the agreement for sale does not enumerate the debt or notes in question in the schedule which purports, according to its heading, to be a statement of assets and liabilities of the old Trinidad Asphalte Company, that schedule is, as appears by Clause 1 of the agreement, an enumeration of matters and things which the vendor warranted to be included in the property sold, or the equivalent in value thereof. Some of the items mentioned in the schedule may have been overvalued, some undervalued, and no doubt fluctuations in value of the assets have supervened, but the amount of this debt is a distinct item of the property purchased which has since been realised by payment. It appears to me that the amount in question is *primâ facie* capital, and that I have no evidence which would justify me in saying that it has changed its character because it has turned out to be of greater value than had

been expected. It was urged for the defendants that the amount applied in payment of the debt was money earned by the Bermudez Company by favour of the defendant company, and represents a profit which would otherwise have been earned by the defendant company, and, furthermore, that such money might have been applied by the Bermudez Company in payment of a dividend on the shares in that company, in which case the defendant company, as owning 9,842 shares out of a total of 10,000 in that company, would have received the greater portion as income. I am unable to follow this argument, as I do not see how for the purposes of the present motion I can have regard to the fact that some other course of dealing by the debtor company would have left the debt still outstanding and would have produced more income for the defendant company. I think that I ought to grant an injunction until judgment or further order to restrain the defendants from distributing the \$100,000 as dividend without reference to the other business or assets of the defendant company. I must not, however, be understood as determining that this sum or a portion of it may not properly be brought into Profit and Loss Account or be taken into account in ascertaining the amount available for dividend. That appears to me to depend upon the result of the whole account for the year. It is clear, I think, that an appreciation in total value of capital assets, if duly realised by sale or getting in of some portion of such assets, may in a proper case be treated as available for purposes of dividend. This, I think, is involved in the decision in the case of *Lubbock v. British Bank of South America* (1892, 2 Ch. 198) cited with approval by Lord Lindley in *Verner v. General and Commercial Investment Trust* (1894, 2 Ch. 239, at page 265), where he says:—"Moreover, when it is said, and said truly, that dividends are not to be paid out of capital the word 'capital' means the money subscribed pursuant to the memorandum of association, or what is represented by that money. Accretions to that capital may be realised and turned into money, which may be divided amongst the shareholders, as was decided in *Lubbock v. British Bank of South America*." If I rightly appreciate the true effect of the decisions, the question of what is profit available for dividend depends upon the result of the whole accounts fairly taken for the year, capital, as well as profit and loss, and although dividends may be paid out of earned profits in proper cases, although there has been a depreciation of capital, I do not think that a realised accretion to the estimated value of one item of the capital assets can be deemed to be profit divisible amongst the shareholders without reference to the result of the whole accounts fairly taken.

(*Times*, 29 November 1900.)

The case *in re* EBENEZER ROBERTS & SONS, LIM.

(Decided before Mr. Justice COZENS-HARDY, in the Chancery Division,
on 28th January 1901.)

*Company Liquidation—Claim for Misfeasance against Directors and Auditors—
Alleged Wilful Negligence—Payment of Dividends out of Capital—Respondents' Right of Contribution inter se.*

This was a misfeasance summons taken out by the liquidator of Ebenezer Roberts & Sons, Lim., against the directors and Auditors of that company. Two of the directors and the Auditors had compounded the claims against them before the hearing of the summons, while as regards the third director (Mr. Hadley Roberts) no answer had been put into the claim, and his Lordship accordingly held him responsible for the whole sum claimed, the figures, if in doubt, to be settled by the Registrar. As regards the remaining respondent (Mr. Baxter), it was alleged that he was not liable, as he had acted in good faith throughout, and had been deceived by his co-directors. The precise facts may be sufficiently gathered from his Lordship's judgment, reproduced below.

JUDGMENT.

Cozens-Hardy, J.: This is a summons by the liquidator, seeking to make Mr. Baxter liable in respect of certain alleged misfeasances while a director. Relief is sought by the summons against the Auditors and the other directors, but as against them the case has been disposed of. The company was formed in the beginning of 1897. Mr. Baxter was not one of the original directors, but he became a director and chairman of the board on the 31st of March 1897. The company was formed to purchase an old-established business of the Roberts family, the purchase-price being £25,000 in cash and certain preference and ordinary shares. The terms of purchase were stated in an agreement dated the 18th of January 1897, referred to in the original prospectus. On the 1st of February there was a supplemental agreement, modifying the terms by providing that the company should take the property subject to an existing mortgage of £3,000, and that the then balance of £9,000 should be taken to some extent in shares, and there was a second supplemental agreement of the 10th of February. On the 10th of February the assignments were executed. On the 14th of April 1897, at a board meeting at which Mr. Baxter was present, it was resolved that a cheque be drawn for £6,900, the balance of the purchase-money. This was done, and the cheque was paid. This payment was correct, if the agreement of the 18th of January had not been modified, but it was not

correct having regard to the supplemental agreements of the 1st and 10th of February. I find, however, as a fact that Mr. Baxter was not aware of the existence of the supplemental agreements, and I cannot hold him liable in respect of this sum.

The summons seeks also to make Mr. Baxter liable in respect of a sum of £1,000 paid to Mr. Hadley Roberts for his invention for ice-powder, called "frigerite." This purported to be a secret chemical process. Such a purchase was authorised by the memorandum of association, clause 3m. The recipe was placed in a sealed envelope, which has been opened by the liquidator, and it is alleged that there is nothing new in it, the process being well known. I cannot, however, hold Mr. Baxter liable for this. He acted in good faith. It is of the essence of a purchase of a secret process that the purchaser should not be able to examine it beforehand. The powder did produce the results claimed. The transaction may have been a fraud on the part of the vendor, but I think Mr. Baxter is free from liability.

The summons also seeks to make Mr. Baxter liable for a sum of about £500, paid in respect of the promotion of a company called Bovo Gravy, Lim. Now, the promotion of a company was *intra vires* this company. I am satisfied from the minutes that the company did promote Bovo Gravy, Lim., and did render itself liable to certain persons in respect of the costs of promotion, and I cannot hold this payment to have been improper, even though it be true that it was contemplated that other persons, who in the event proved unable to discharge their obligations, should bear the liability.

I do not pause to consider a loan of £500 made to a company without any security. It may have been imprudent, but it was not *ultra vires*; nor do I think there was any want of good faith on the part of Mr. Baxter.

It only remains to consider one other matter raised by the summons, which presents considerable difficulty. It is alleged that a sum of £4,077 13s. 8d. was paid in respect of the year 1897 as dividend, though there were no profits applicable for the purpose, the dividend being paid out of capital. The material facts are these. On the 25th June 1897 the following resolution was passed:—"With reference to the payment of half-yearly dividend on preference shares, it was resolved, on having gone into the calculation of profits made on the sale of patent freezers and imperial ice-cream powders, as under, and finding ample profit would have been made to declare an interim dividend of 6 per cent. per annum on amount of paid-up preference shares allotted, interest to be calculated as from

date of payment of instalments—Resolved to close the list of shareholders from the 30th of June to the eighth day of July, and that the same be advertised. The managing director reported that — patent freezers and — imperial ice-cream powders had been sold to date.” These blanks in the minutes were never filled up, and Mr. Baxter says he declined to sign the minutes on the very ground that the blanks were not filled up. Nevertheless, an interim dividend, amounting to £1,039 6s. 6d. was paid on the preference shares.

The accounts for the year 1897 were sent to the shareholders with the directors' report on the 24th of February 1898. They purported to show a net profit of £5,017 11s. 1½d., from the balance of which, after deducting the interim dividend, the directors recommended a dividend of £6 per cent. on all the shares, both preference and ordinary. This account is certified by the Auditors in the following terms:—“We have examined the books of the above company for the year ending 31st December 1897, and the vouchers connected therewith, and hereby certify the above figures to be in accordance with the same.” This certificate was not such as was required by Articles 161 and 166, which are as follows:—161.—“Once at least in every year the accounts of the company shall be examined, and the correctness of the Profit and Loss Account, and Balance Sheet, ascertained by an Auditor or Auditors.” 166.—“The Auditors shall make a report to the members upon the Balance Sheet and Accounts, and in every such report shall state whether in their opinion the Balance Sheet is a full and fair Balance Sheet, and properly drawn up so as to exhibit a true and correct view of the state of the company's affairs, and such report shall be read, together with the report of the directors, at the meeting at which the Balance Sheet is submitted.” It is proved to my satisfaction that there were no profits available for this dividend. It is plain that gross frauds were committed by one or other of the two managing directors, although I exempt Mr. Baxter from any imputation of fraud. In particular, two sums of £540 12s. and £2,214 11s. 9d., entered as assets, were fraudulent items inserted in the books without anything representing them. I cannot, however, having regard to the *Kingston Cotton Mills* case, hold Mr. Baxter liable for not having discovered these frauds. He did not suspect, and, so far as I can see, he had no reasonable grounds for suspecting, the integrity of his colleagues on the board. With respect to an item of £556 4s. 8d., which represents the nominal amount of the book debts of the vendors in excess of the nominal amount of their liabilities, this sum, if it had any existence, was purchased and paid for by the company under the agreement of January 1897. It was capital, and not in any way part of the profits of the company, or available for dividend. In fact, it had no existence, for these debts were, to a very

large extent, bad, and the liabilities were far greater than the books showed. There was, I think, no justification for dealing with this item in the manner in which it was dealt with. Moreover, a glance at the books of the vendors would have shown that the greater part, if not all, of the debts represented by the £566 4s. 8d. were bad. Another item in the Balance Sheet is an assumed profit of £1,250 in respect of Numan & Stove, Lim. This was a company registered in June 1897. Mr. Baxter was one of its directors. It was promoted by the International Securities Trust Corporation, Lim. On the 29th of June 1897 the following resolution was passed:—"It was resolved that £500 be advanced as a temporary loan towards the formation of a syndicate for the issue of Numan & Stove, Lim., as per agreement, and for reasons and considerations given—namely, in consideration of this company advancing as a temporary loan the sum of £500 to the International Securities Trust Corporation, Lim., towards the formation of Numan & Stove, Lim., whose managing director undertook to keep stock and push sales in every possible way amongst the various steamship companies, wherein their business lies, of the company's patent freezers and imperial ice-cream powders, and the undertaking entered into by the managing director of the International Securities Trust Corporation, Lim., for his company to be personally responsible for the return of the said £500, they lodging with the company scrip for 1,000 ordinary £1 shares in Ebenezer Roberts & Sons, Lim., together with a bonus of £500 in cash or preference shares, and 1,000 fully-paid ordinary shares in Numan & Stove, Lim." And on the same day the following letter was written by the International Securities Trust Corporation, Lim.:—"In consideration of your advancing the sum of £500 towards the expenses of forming Numan & Stove, Lim., and issuing the prospectus offering 7,500 preference shares of £5 each and 750 founders' shares of £1 each for subscription, we hereby guarantee the return to you of the said sum by the vendor, Mr. A. E. Stove, out of the first moneys payable by him under his agreement of sale, after £1,000 to pay off mortgages and £2,000 for the company's working capital. In the event of his not receiving sufficient from the subscriptions to repay you the said sum, we undertake to make up any deficiency, and as security for the present engagement we herewith lodge with you £1,000 of ordinary shares of your company as collateral security. In addition to the above, in the event of the company proceeding to allotment, you are to receive as bonus £500, either in cash or in preference shares, whichever is available as the result of the subscriptions, and £1,500 in ordinary shares of Numan & Stove, Lim. These latter payments, though we will do our best to see carried out, are not guaranteed by us." The £500 was advanced. In the result it has been a total loss.

On the 8th of October 1897 the secretary of the International Securities Trust Corporation, Lim., wrote to this company, informing it that "the subscriptions were not sufficient to allow Mr. Stove to receive cash to enable us to return you the amount in cash. We therefore enclose you 100 preference shares of £5 each for the amount. We also send you 100 preference shares of £5 each and 1,500 ordinary shares of £1 each as agreed bonus." This letter showed that Numan & Stove, Lim., had not been a success. The company in the Balance Sheet treated the £500 as a good loan, amply secured, and they treated the shares, which were the agreed bonus, as worth £1,250. In other words, they treated the preference shares as of par value, and the ordinary shares as worth 50 per cent. of their face value. These shares had no market value. Mr. Baxter says that he objected to the value put upon the shares unless a statement could be obtained from the secretary as to their value, but no such statement was obtained until shortly before the 1st of April 1898, and the letter then obtained, which asserted that the shares were at present of par value, was ante-dated the 23rd of December 1897. The resolution for payment of the dividend was long before this letter was received. Mr. Baxter was a director of Numan & Stove, Lim., until November 1897, when he resigned his seat because he was not satisfied with the conduct of his colleagues. In my opinion, there was no justification for treating this transaction as one resulting in a profit of £1,250. In truth, the shares have proved wholly worthless, the company being wound up in 1898.

In addition to the four items above-mentioned, the liquidator points out that under the item £3,172 2s. 4d., By new machinery, which is a capital item, there are included items amounting to £467 18s. 3d., which clearly ought to be placed to the debit of profit and loss, and that, in like manner, in the item Establishment Account £580 15s. 1d., there are included items amounting to £443 1s. 6d., which are plainly not capital charges. I may add that, in order to provide for the first dividend, money had to be borrowed from the company's bankers. Under these circumstances it is contended by the liquidator that Mr. Baxter, although not guilty of fraud, has been so careless and negligent in the discharge of his duty as director that he should be held liable for the total amount of the dividend paid, or at least for so much as could not have been paid if the items above referred to, other than the two fraudulent items, had been struck out; and it is argued that he cannot rely upon any protection which might have been afforded by the certificate of the Auditors, inasmuch as they did not in fact, nor did they even profess to, do their duty—namely, ascertain the correctness of the Profit and Loss Account and Balance Sheet, or state whether it exhibited a true and correct view of the state of the company's affairs.

On the other hand, it is contended by Mr. Baxter that he was not bound to go through the books, that he was entitled to rely upon the managing directors who in the first instance had prepared the Balance Sheet, and upon the Auditors who certified it, and that he, not unreasonably, attached no importance to the omission of the Auditors to give the full form of the certificate prescribed by the articles.

Now, with regard to the dividend, I think I ought not, in the present state of the authorities, to hold Mr. Baxter responsible (a) in respect of the two fraudulent items of £540 12s. and £2,214 11s. 9d., or (b) in respect of the £556 4s. 8d. book debts, or (c) in respect of items wrongly included in New Machinery and Establishment Accounts. These last items were passed by the Auditors, and I regret that I must hold that Mr. Baxter was not bound to look at the books which would have disclosed the true fact. Although the Auditors were, in my judgment, culpably negligent, not only in treating item (b) as a good asset, but also in failing to distinguish between capital and income in items (b) and (c), and although Mr. Baxter omitted to require the Auditors to give the prescribed certificate, this does not suffice to render him pecuniarily responsible. See the observations of Vaughan Williams, J., in the *Kingston Cotton Mills* case (1896, 1 Ch. 348).

But there are two matters in respect of which I cannot hold Mr. Baxter free from responsibility. He was a party to the payment of the interim dividend, recklessly and without obtaining the information which he knew was necessary to justify it. The blanks in the minute of the 25th January were never filled up. There was no such calculation of profits made as there stated. In the result, it is shown that no profits were in fact made, and I must, therefore, hold Mr. Baxter liable for £1,039 6s. 6d., the amount of the interim dividend.

With respect to the final dividend, amounting to £3,038 7s. 2d., it is admitted that this depends upon the Numan & Stove item, £1,250. Now, it is clear that Mr. Baxter was well acquainted with the affairs of that company. He knew that it was not flourishing. He retired from the board in November 1897, as he says, because he did not trust his co-directors. He knew that some evidence of value was required to justify the figures, and yet he sanctioned the dividend without obtaining any such evidence. I decline to accept his statements in the box that he believed then that the shares were worth £1,250, and that he himself would have given that sum for the shares. He acted recklessly, although his attention was expressly drawn to this item. The accounts purported to show £5,017 11s. 1½d. profits for the year. From this must be deducted the interim dividend, £1,039 6s. 6d., and also the £1,250.

This leaves only £2,728 4s. 7d. available for the final dividend. But the dividend paid amounted to £3,038 7s. 2d., an excess of £310 2s. 7d. I must hold Mr. Baxter liable for this sum of £310 2s. 7d., in addition to the £1,039 6s. 6d., making in all £1,349 9s. 1d., and he must pay interest at 4 per cent. on each sum from the date of payment by the company. He must pay the costs of the summons. I have not had an opportunity of looking at the order sanctioning the compromise with the directors and the Auditors. I do not think that that will be in any way material to this.

Mr. Eve: Are not we entitled to credit for anything received, my Lord?

Cozens-Hardy, J.: No; I think not.

Mr. Eve: It is not a very large amount. Your Lordship's judgment will be for £1,349 9s. 1d., with 4 per cent. interest on the one sum from the date of the interim dividend when declared, and also on this latter sum, with costs.

Cozens-Hardy, J.: I did not go into the sum. You can work it out.

Mr. Eve: If your Lordship pleases.

Cozens-Hardy, J.: The interest will be inserted in the order.

Mr. Eve: Yes, my Lord, the amount will be calculated and inserted in the order.

Cozens-Hardy, J.: You do not appear for Roberts. I understand, Mr. Martelli, the order was taken there?

Mr. Eve: Yes, my Lord, the order was taken.

Cozens-Hardy, J.: The summons asks in the alternative; it did not prescribe which alternative. I do not suppose it matters.

Mr. Martelli: When my learned friend was opening this case I think we thought the larger sum—that is, the amount paid altogether in excess—but that was probably more than your Lordship would give us, and then we put an intermediate sum.

Cozens-Hardy, J.: The excess of the purchase-money is plainly what they are liable for. The first item I dealt with in my judgment was £6,900—was not that the amount of the cheque paid?

Mr. Martelli: Yes, my Lord, £6,900.

Cozens-Hardy, J.: I do not know the amount by which it was in excess, but it was in excess to a considerable extent, having regard to the modified agreement.

Mr. Martelli: Your Lordship remembers that the total amount was £3,336; that was paid on the 5th of May, but under the agreement the view was that they were entitled to credit for all the shares allotted up to the 31st of January, which was something less than that. The figures I gave your Lordship were £2,383, that is allowing them the benefit of shares allotted between the 5th of May and the 31st of January. That is rather a less sum than is claimed by the summons, but rather more than the second alternative. The second alternative gave them credit for all shares allotted at any time.

Cozens-Hardy, J.: That cannot be right.

Mr. Eve: Your Lordship decided that. I was arguing it as *amicus curiæ*.

Cozens-Hardy, J.: Yes; I decided that.

Mr. Martelli: The proper amount will be giving them credit for all shares allotted up to the 31st of January, which they were entitled to under the agreement.

Cozens-Hardy, J.: Have I got the materials before me to insert the figure for that?

Mr. Martelli: Yes; your Lordship sees it is strictly proved in the affidavit which I gave your Lordship. The figure will be £2,383.

Cozens-Hardy, J.: Very well; put that in the order.

Mr. Martelli: That is £1,000 less than we claim.

Cozens-Hardy, J.: That will be with interest, of course.

Mr. Martelli: That will be with interest from the 31st of January, anyhow, giving them the benefit up to then.

Cozens-Hardy, J.: Yes; take it most favourably to them.

Mr. Martelli: That is the most favourable view we can take in their favour, £2,383. Then will your Lordship allow the dividend?

Cozens-Hardy, J.: They are liable for the fraudulent items. What does Mr. Eve say as *amicus curiæ*?

Mr. Eve: Yes; I think so. The whole dividend, as far as they are concerned.

Mr. Martelli: I do not think we can ask for anything more.

Mr. Eve: Yes; that exhausts it.

Cozens-Hardy, J.: I do not suppose it matters what judgment I give against them?

Mr. Eve: I do not want to reply on your Lordship's judgment, but may I ask your Lordship, in arriving at the £310 2s. 7d., ought not my clients to have had credit for the £1,000, the interim dividend, which

under this judgment we replace? The supposition is that under the judgment we replace that £1,039 in the company's coffers. If that was so, ought that to have been deducted from the profits ascertained at the end of the year?

Cozens-Hardy, J.: The interim dividend is one thing, and the final dividend is another. There was no justification at all for the interim dividend.

Mr. Eve: If it is replaced in the company's coffers there would be £1,039, which, assuming the judgment is complied with, goes to our credit. However, if your Lordship has taken that into consideration—

Cozens-Hardy, J.: I have let you off very easily.

(*Acct. L.R.*, 1901, p. 43.)

The case of HERBERT ALFRED BURLEIGH *v.* INGRAM
CLARK, LIM.

(Decided before Mr. Justice JOYCE, in the Chancery Division, on April
2nd 1901.)

Held that an Accountant has a Lien on Account Books for Professional Charges.

Mr. Lawrance said he had a motion in the case of Herbert Alfred Burleigh, of Park Row, Bristol *v.* Ingram Clark, Lim., booksellers and stationers, of Bristol, against the Auditor of the defendant company for an order upon him to hand over the account books of the company to the receiver appointed in a debenture-holder's action. The motion raised a very nice point, and one as to which, as far as he knew, there was no authority whatever—namely, whether the Auditor of a company had a lien on the books of the company for his fees. The receiver (Mr. Frederick Jenkins, F.C.A.) was appointed on the 8th of February last in the action by Mr. Burleigh on behalf of himself and other first debenture-holders for £7,000, and Mr. W. Grimes, A.C.A., the Auditor, was requested to go into the accounts. He now took the view that he had a lien on the books of the company for work done, and he refused to deliver up the books except on payment by the receiver of his account, £137. The way in which he got possession of the books was this. He asked leave of the directors and the secretary to take away the books to his own office, as he said the company's office was small and inconvenient for him, and he could do the work better in his own office.

Mr. Christopher Jones, for the accountant, said if the money was brought into Court he would hand over the books at once.

Mr. Lawrance said that was just what he contended the Auditor was not entitled to.

Mr. James pointed out that Mr. Grimes had done accountant's work to the books, as well as Auditor's work.

Mr. Lawrance admitted that some work had been done on the books, as distinguished from work done in respect of the books, and there might be a distinction. He did not think his Lordship at present had got the materials for saying how much was actually done on the books, and how much done in the books. He contended that the Auditor had no lien for any part of the work. If he had, then there must be some inquiry. He thought if there was such a thing as an Auditor's lien on the books he worked upon, it must have been tried on before, but he could not find any record.

Joyce, J., said he had no evidence here as to the terms upon which the Auditor was employed. There might be some resolution of the board, and it was very material to know on what terms he was employed. He might have been employed as accountant, as well as Auditor.

Mr. James said there was the evidence of Mr. Grimes himself that he was asked by the board of directors to do this accountant's work.

Mr. Lawrance contended that the company, by allowing the Auditor to take away the books for his own convenience, conferred on him no right to retain them. He was appointed Auditor in the usual way, yearly. He admitted Mr. Grimes had bought a Shareholders' Register, an important book, for the company, and that the receiver had not yet paid him the price, 31s., but the receiver would see that that was paid.

Mr. James, in opposing the application, said it might be that work done as an accountant and work done as an Auditor stood on different footings, but he contended, in any event, the Auditor had a lien. The bulk of the work was done as an accountant, and so far as that branch of the work went he clearly had a lien on the authorities. The right of an Auditor was, no doubt, somewhat different, but even in that case he submitted there was a lien.

Joyce, J., said, apart from other matters, it was clear the Auditor had no right to keep the Shareholders' Register, as that was a book which the company must keep for public inspection, and he must therefore give it up. That was not an account book. As to the articles of association, he could not see that the article relating to the Auditor gave him any lien whatever on the books. At present he was of opinion that no book of the company ought to leave the company's office.

Mr. James said if these books had to be re-bound the binder would have a lien on them for his work.

Joyce, J., said he did not know, but he thought if a parish register had to be re-bound it could not be detained.

Joyce, J., asked Mr. Lawrance whether, if the Auditor would return the books at once, the receiver would be willing to give the Auditor a personal undertaking to pay whatever it might be found he was entitled to. Of course, he did not say that the Auditor was entitled to a lien.

Mr. Lawrance consulted his clients, and said they were willing to give that undertaking.

Joyce, J., said, Very well! This was obviously an urgent matter, because the company must have its books, and this arrangement would settle the matter temporarily. If the books were handed over and the undertaking given, he would postpone his decision as to the law until the first day of next sittings, because he wished to look at the documents, as this was a novel point.

JUDGMENT.

His Lordship delivered judgment on the 18th inst. He said that the affidavits filed showed that the respondent claimed a lien, not as Auditor, but as accountant. In his opinion, the question of an Auditor's lien did not arise, and, had it done so, he considered that an Auditor had no such lien; but that point he did not now decide. In respect of the Share Register, the accountant had no possible lien on that, but he held that he was entitled to a lien on such books only as he had actually worked upon, in respect of his proper remuneration for work upon those books only. If the parties did not agree upon the sum, there must be an inquiry. Each side would pay its own costs.

(*Acct. L.R.*, 1901, p. 65.)

The case of DOVEY AND OTHERS *v.* CORY (NATIONAL BANK OF WALES CASE).

(Decided by the House of Lords, before the LORD CHANCELLOR, LORD MACNAGHTEN, LORD SHAND, LORD DAVEY, and LORD BRAMPTON, 1st August 1901.)

Held that a Director, if he acts bonà fide, is entitled to rely on the Officers of the Company to prepare true and honest Accounts.

This was an appeal from a decision of the Court of Appeal (the Master of the Rolls, now Lord Lindley, Sir F. H. Jeune, and Lord Justice Romer), dated August 2 1899, which reversed a judgment of Mr. Justice Wright, dated February 27 1899. The hearing before the

Court of Appeal is reported in XXV. *Acct. Law Reports*, 127; 15 *The Times Law Reports*, 517; L.R. (1899), 2 Ch. 627; and 68 L.J. Ch. 634.

The appellant is the liquidator of this bank, and the Metropolitan Bank (of England and Wales) have purchased and taken over its assets and liabilities. The respondent, John Cory, was for some years a director of the National Bank. In the liquidation of the latter a summons was taken out to render the respondent liable—not to creditors, all of whose claims had been satisfied, but to the contributories, in respect of alleged misfeasance (1) in paying dividends out of capital; (2) in making improper advances to directors; and (3) in making improper advances to customers who were, or were reputed to be, insolvent, and the summons asked that the respondent should be ordered to repay the full amount of all losses caused by such acts of alleged misfeasance with interest and costs. Mr. Cory became a director on November 23 1883, and resigned on December 18 1890. The summons asked that the respondent should be deprived of the benefit of the Trustee Act 1888, and of the Statutes of Limitation, on the ground that the losses arose from the respondent's wrongful acts and fraudulent concealment of the true state of affairs. The appellant's counsel, however, disclaimed the imputation of any moral obliquity on the part of the respondent, but argued the question on the basis of negligence and failure to discharge the duties of a fiduciary position. The transactions complained of were voluminous, and ranged over a series of years, and related to the affairs not only of the head office, but of the branches, which in 1890 were 33. It was, however, found possible by the parties to condense the story within the limits of four volumes and about 1,500 pages. In February 1893 an agreement was entered into between the National Bank of Wales and the Metropolitan, Birmingham, and South Wales Bank, now the Metropolitan Bank (of England and Wales), Lim., whereby the latter bought the assets and goodwill and undertook the liabilities and contracts of the former, the value of the assets and goodwill being taken at not less than £110,000. Voluntary resolutions were passed for winding up the National Bank, and Thomas Cory, its former chairman, and the appellant were appointed liquidators. Mr. Thomas Cory subsequently resigned and the appellant became sole liquidator. The alleged amount of improper payments of dividends was £52,986; of loss on advances and credits to directors to December 31 1890, £37,731; and of loss on improper advances to customers, £43,087. The whole of the assets were realised or valued, and the appellant Dovey alleged that after discharging the liabilities of the National Bank and crediting it with the value of its assets and £110,000 as its goodwill, there remained a deficiency of assets amounting to £84,392. Calls were made of £2 10s. per share each in July

1896 and September 1899. Mr. Justice Wright ordered the respondent to pay £54,787, being £37,000, the aggregate amount of dividends paid to the shareholders in 1887, 1888, 1889, and 1890 (except a part of the last dividend), and as to the balance, interest at 5 per cent. on each of the dividends. The learned Judge held that all these dividends were in fact paid out of capital; but he declined to make the respondent liable for improper advances to directors or customers. The Court of Appeal, in an elaborate judgment, delivered by the Master of the Rolls, exonerated the respondent from liability. This decision was affirmed by the noble and learned Lords.

JUDGMENT.

The Lord Chancellor: In this case the liquidator of the National Bank of Wales, Lim., appeals against a judgment of the Court of Appeal, whereby Mr. John Cory, the respondent, was discharged from the liability which Mr. Justice Wright's judgment had imposed upon him to pay £37,000 for the benefit of the shareholders of the company in respect of dividends already distributed, and a further sum for interest. Mr. John Cory was a director of the company, and it is for his supposed misconduct in the management of the affairs of the company that this liability was imposed upon him. It is alleged and proved that certain losses have been sustained by the company, and the ground upon which Mr. John Cory is sought to be made liable is the very short and intelligible ground that he was a party to false and fraudulent statements as to the position of the company, and had had a share in causing these losses. The Court of Appeal have acquitted him of any knowledge of what was falsely stated, and Sir Robert Reid, in opening this appeal, stated to your Lordships that he did not intend, in arguing for Mr. John Cory's liability, to impute to him any moral obliquity. Now, there is no doubt that there were Balance Sheets laid before meetings of the shareholders which, to use the language of the articles of association, were not proper, and which did not truly report as to the state and condition of the company, and did not comply with the requirements of the articles in question in respect of the particular sum which the directors recommended as dividend, that it should be paid out of the profits, but a greater sum was paid out as dividend than would have been paid if certain things had been taken into consideration, and therefore larger than should have been paid. A great part of the judgment, both of Mr. Justice Wright and of the Court of Appeal, is occupied by discussing matters which are not now before your Lordships as matters in debate. It is now admitted that Mr. John Cory ceased to be a director in December 1890. My Lords, I am very clearly of opinion that the judgment of the Court of Appeal is right and ought to be affirmed; but my opinion is entirely based upon the question of

fact that he was guilty of no breach whatever, and for reasons which I will refer to hereafter I am very anxious not to deal with some reasons given for their judgment by the Court of Appeal, which, in the view of the facts that I take, do not arise here; and in what I say I desire to be understood as only dealing with the facts of this particular case. Now, in the first instance, I will assume that the company has sustained loss by the issue of fraudulent Balance Sheets, by the improper advance of money to the customers of the bank, and that it has also sustained loss by the lending of money to directors without security. With respect to the default involving liability, if Mr. John Cory was conscious of the falsehood it is not necessary to go any further. Like anyone else who is a party to a false statement acted upon to the prejudice of the person to whom it is made, he would be liable to the extent to which his falsehood has inflicted loss on his victims, but after the admission that has been made it is unnecessary to pursue this head of inquiry; he certainly could not be acquitted of moral obliquity if party to a fraudulent statement; but it is said he has so grossly neglected his duty as a director that, though he may not have known the true state of the facts, he ought to have known them, and his breach of duty in that respect renders him liable. In order to see how far this obligation is made out it is necessary to consider what the business of the company was, and what was the position of Mr. John Cory in relation to it. My Lords, I think it is idle to talk in general terms of the duty of a director to look after the concerns of the company of which he is one of the managers without seeing what in the ordinary course of business he ought to do or to have done. Now, there are some things which, of course, must be, or at all events ought to be, apparent to anyone responsible for the conduct of a commercial business, and to apply that observation to the business of which we are speaking—namely, a banking business; but I do not understand that anyone has suggested that there was neglect or default by reason of the absence of some system under which, if honestly carried out, the interests of the bank would have been in that respect secured. It is admitted that (extract from judgment of the Court of Appeal) “the company’s principal bank and its head office were at Cardiff, where the directors met and the general manager was in daily attendance. The company had also many branch banks each with its own manager. The course of business was this. Each branch manager sent weekly to the head office what is called a weekly state—*i.e.*, an account showing how the assets and liabilities of the branch stood, what advances or overdrafts had been made or allowed and to whom, what securities the bank held, and other matters. Every quarter each branch manager made a more formal return to the head office showing the position of the branch and the business done during the past quarter. It was the duty of

the general manager to examine these documents, and to report to the board anything disclosed by them which required their attention. The weekly states or quarterly returns were in the board room for reference in case of need, but unless attention was called to them the directors did not think it necessary to examine them. The chairman of the directors was Mr. Thomas Cory, a brother of Mr. John Cory. The chairman and the general manager (Mr. Collins) visited each branch bank every year; and, in addition, two skilled inspectors frequently went round and inspected the accounts and reported to the general manager. The accounts of the branch banks appear, however, not to have been separately audited by professional accountants. The Auditors employed to examine the company's accounts and to certify the annual Balance Sheets and accounts laid before the shareholders only saw the head office books and the returns from the branch offices certified by their respective managers to the head office. These certified returns formed part of the weekly states, but omitted much that they contained. The minutes of the directors' meetings show that, speaking generally, they attended with reasonable regularity and transacted a large amount of business. No director, unless it was the chairman, attended to any details not brought before the board either by the chairman or by the general manager. Mr. John Cory stated in his affidavit the general course of business at board meetings, and his cross-examination does not substantially differ from the account he there gives." But it is suggested that Mr. Cory is responsible because this and other portions of the system were not faithfully adhered to. And, indeed, what is really made the test of his responsibility is that he did not find out what was fraudulently withheld from his knowledge. So the warning letters of the Auditor, which were never suffered to reach him, are suggested as warnings to him which he ought not to have neglected. Again, the insufficient striking out of bad and doubtful debts, by which it is alleged that the amounts paid in dividends to himself and other directors, as well as shareholders, are by a process of reasoning and calculation assumed to be payments out of capital. These things are all assumed to have been done as though done with knowledge and intention, while at the same time the admission is made that there was no evil mind or conscious fraud. Now I think such things, if done with evil mind and intention, would be fraud, and it comes back again to the proposition that the responsibility must be based upon the assumption that Mr. Cory is responsible because he did not find out the fraudulent knaves by whom he was surrounded. One was his own brother, another was the general manager, and, once I arrive at the conclusion that there were those about him whose interest and object it was to deceive him, I certainly do not think that the

things which were designedly concealed from him are things which ought to be relied upon as matters for which he was responsible. In the view I take the whole of the evidence which is relevant and important to the question "Did Mr. Cory knowingly permit the things to be done which were done?" becomes to my mind entirely immaterial if one is to start with the assumption that he knew nothing about them. Dealing with the several heads of charge as they have been formulated in the judgment of Mr. Justice Wright—viz., negligence, breaches of trust in respect of advances made contrary to said articles of association, and payment of dividends and of capital—I think each and all of them may be disposed of by the proposition that Mr. Cory was not himself conscious of any one of these things being done, and that unless he can be made responsible for not knowing these things—or, as Mr. Justice Wright put it, he is shown to have exhibited a complete neglect of the duties he had undertaken—the charges are not made out. The charge of neglect appears to rest on the assertion that Mr. Cory, like the other directors, did not attend to any details of business not brought before them by the general manager or the chairman, and the argument raises a serious question as to the responsibility of all persons holding positions like that of directors—how far they are called upon to distrust and be on their guard against the possibility of fraud being committed by their subordinates of every degree. It is obvious if there is such a duty it must render anything like an intelligent devolution of labour impossible. Was Mr. Cory to turn himself into an Auditor, a managing director, a chairman, and find out whether Auditors, managing directors, and chairmen were all alike deceiving him? That the letters of the Auditors were kept from him is clear. That he was assured that provision had been made for bad debts and that he believed such assurances is involved in the admission that he was guilty of no moral fraud; so that it comes to this—that he ought to have discovered a network of conspiracy and fraud by which he was surrounded, and found out that his own brother and the managing director (who have since been made criminally responsible for frauds connected with their respective offices) were inducing him to make representations as to the prospects of the concern and the dividends properly payable which have turned out to be improper and false. I cannot think that it can be expected of a director that he should be watching either the inferior officers of the bank or verifying the calculations of the Auditors themselves. The business of life could not go on if people could not trust those who are put into a position of trust for the express purpose of attending to details of management. If Mr. Cory was deceived by his own officers—and the theory of his being free from moral fraud assumes under the circumstances that he was—there appears to me to be no case against him at all. The provision made

for bad debts, it is well said, was inadequate, but those who assured him that it was adequate were the very persons who were to attend to that part of the business—and so of the rest. If the state and condition of the bank were what was represented, then no one will say that the sum paid in dividends was excessive. If I assume, as I do, that Mr. Cory acted upon representations made to him which he believed and which as coming from the officers of the bank to whom he was, in my judgment, justified in giving credit, the discussion of whether the dividends actually paid were or were not properly divisible, has no bearing on Mr. Cory's liability, and I am very reluctant to give any opinion upon it, inasmuch as the question may arise when it may be necessary to decide it. I deprecate any premature judgment. My Lords, I am, as I have said, very reluctant to enter into a question which for the reasons I have given does not arise here, and into which the Court of Appeal has entered at some length. The only reason why I refer to it at all is lest by silence I should be supposed to adopt a course of reasoning as to which I am not satisfied that it is correct. I doubt very much whether such questions can ever be treated in the abstract at all. The mode and manner in which a business is carried on, and what is usual or the reverse, may have a considerable influence in determining the question what may be treated as profits and what is capital. Even the distinction between fixed and floating capital, which in an abstract treatise like Adam Smith's "Wealth of Nations" is appropriate enough, may with reference to a concrete case be quite inappropriate. It is easy to lay down as an abstract proposition that you must not pay dividends out of capital, but the application of that very plain proposition may raise questions of the utmost difficulty in their solution. I desire, as I have said, not to express any opinion, but as an illustration of what difficulties may arise the example given by the learned counsel in one ship being lost out of a considerable number, and the question whether all dividends must be stopped until the value of that lost ship is made good out of the further earnings of the company or partnership, is one which one would have to deal with. On the one hand, people put their money into a trading concern to give them an income, and the sudden stoppage of all dividends would send down the value of their shares to zero, and possibly involve its ruin. On the other hand, companies cannot at their will and without the precautions enforced by the statute reduce their capital; but what are profits and what is capital may be a difficult and sometimes an almost impossible problem to solve. When the time comes that these questions come before us in a concrete case we must deal with them, but until they do, I, for one, decline to express an opinion not called for by the particular facts before us, and I am the more averse to doing

so because I foresee that many matters will have to be considered by men of business which are not altogether familiar to a Court of law. I move that this judgment be affirmed, and this appeal dismissed with costs.

Lord Macnaghten: I have had an opportunity of reading in print the judgment of my noble and learned friend on the Woolsack, and I desire to express my concurrence in it, and at the same time to guard myself from being understood to assent to all the propositions supposed to have been laid down by the Court of Appeal in this case. I say no more, because it seems to me that when Sir Robert Reid withdrew all charges involving moral obliquity against Mr. Cory, the case was at an end. And I do not think it desirable for any tribunal to do that which Parliament has abstained from doing—that is, to formulate precise rules for the guidance or embarrassment of business men in the conduct of business affairs. There never has been, and I think there never will be, much difficulty in dealing with any particular case on its own facts and circumstances, and, speaking for myself, I rather doubt the wisdom of attempting to do more. I understand from my noble and learned friend Lord Shand that he also takes this view.

Lord Davey: I agree with your Lordships in thinking that the appellant has not succeeded in making out a case for the relief which he asks against the respondent. The appellant seeks to make the respondent liable under three heads—(1) in respect of losses incurred by advances of money which he alleges that the respondent and the other directors of the bank negligently made to irresponsible persons, and without sufficient security; (2) in respect of advances to the directors themselves, which he alleges were made contrary to the express provisions of the articles of association; (3) in respect of sums paid to the shareholders (including the respondent himself) by way of dividend on their shares, which he alleges were paid out of the capital of the bank, and not out of profits. In fact he alleges that there were no profits out of which such dividends could properly be paid, and that an apparent profit was created only by including as assets debts known to be bad and irrecoverable. As regards the first two heads of claim, Mr. Justice Wright, as well as the Court of Appeal, has held that the claims cannot be sustained, and as I agree with the reasons which have been assigned for so holding I need not trouble your Lordships by repeating them. As regards the third head of claim, the case as presented at your Lordships' bar has been very much narrowed by the admission of the appellant's counsel that the respondent ceased to be a director in December 1890, and his acceptance of the decision of the Court of Appeal that the Statute of Limitations applies so as to

bar the recovery of any sums paid away prior to six years before the commencement of the proceedings. The claim is thus confined to the three dividends paid in July 1889, December 1889, and July 1890. My Lords, I think it appears from the evidence that in the Balance Sheets upon which these dividends were recommended by the directors bad and irrecoverable debts were in fact included amongst the assets of the company, and that if those debts had been written off (as they ought to have been) the Balance Sheets would not have shown any profit out of which the dividends could have been paid. But before proceeding to discuss the evidence upon which it is sought to fix the respondent with responsibility, I will say a few words with regard to the law upon the subject with a view to ascertain exactly what it is the appellant must establish. After analysing and discussing several authorities, his Lordship proceeded:—The respondent, in his affidavit, states generally that he was from first to last under the honest and genuine belief that the affairs of the company were in a sound and solvent condition, and that its business was being carried on at a profit, and that its net profits for the time being were amply sufficient to justify the dividends which were from time to time during his directorship paid to the shareholders. And he adds that the general manager and branch managers were, so far as he knew, men of unquestioned competence and integrity, and that he and his co-directors were compelled by the magnitude of the business and the exigencies of the case generally to rely upon (and he did rely upon) these officials in all ordinary matters relating to the accounts of customers and other questions of detail. And he deals specifically with the various matters alleged in the liquidator's evidence on the same lines. The respondent was cross-examined on his affidavit at great, but not unnecessary, length. I am not, I think, doing injustice to the appellant's case when I say that reliance was chiefly placed on the "weekly states" and "quarterly returns" made by the branch managers, or that, if he cannot succeed in fixing the respondent with liability on these documents, his case fails. These returns were laid on the table in the board room at each meeting of the directors. The comparative analysis of them, made by the skilled accountant who advises the appellant, does, I think, show that certain accounts which were treated as good by the general manager in the preparation of the Balance Sheets submitted by him to the directors were, in fact, irretrievably bad, and it is difficult to acquit the general manager of improper conduct in including them as assets. The respondent says in his affidavit that the "weekly states" consisted each week of a very large and voluminous pile of sheets, which it would have taken the directors a couple of days to go through, and that it was the duty of the general manager to go through the weekly states,

with the letters of the branch managers accompanying them, and to place upon the agenda any points arising upon them which he considered ought to be brought to the attention of the directors; and upon the discussion of such points the documents were, when necessary, referred to; but, except in such cases, the weekly states were not consulted by the directors, but they relied on the general manager going carefully through them and drawing their attention to any matter requiring their consideration. On cross-examination he adhered to this statement. He added that the chairman also went through them often individually, and he did so for the board. He admitted that before recommending a dividend he did not look at all the accounts or look at the books themselves, but he said that the directors looked at the documents which were put before them by the manager—the amount which he considered was doubtful and bad—and they made a reserve for it. He also said that it was never brought before him that amounts due from bankrupt debtors were included in the Balance Sheet of each year, and he never heard of any single case of that kind. It further appeared from the evidence of other witnesses that the branches of the bank were regularly visited and their books examined by the chairman and two inspectors. In this state of the evidence, I ask whether the course of business at the board meetings as described by the respondent was a reasonable course to be pursued by the respondent and other directors, or whether the knowledge which might have been derived from a careful and comparative examination of the weekly states and quarterly returns from the different branches of the bank ought to be imputed to the respondent, or, alternatively whether he was guilty of such neglect of his duty as a director as would render him liable to damages? I do not think that it is made out that either of the two latter questions should be answered in the affirmative. I think the respondent was bound to give his attention to and exercise his judgment as a man of business on the matters which were brought before the board at the meetings which he attended, and it is not proved that he did not do so. But I think he was entitled to rely upon the judgment, information, and advice of the chairman and general manager, as to whose integrity, skill, and competence he had no reason for suspicion. I agree with what was said by Sir George Jessel in *Hallmark's* case (9 Ch.D. 329), and by Mr. Justice Chitty in *In re Denham & Co.* (25 Ch.D. 752), that directors are not bound to examine entries in the company's book. It was the duty of the general manager and, possibly, the chairman to go carefully through the returns from the branches, and to bring before the board any matter requiring their consideration, but the respondent was not, in my opinion, guilty of negligence in not examining them for himself, notwithstanding that they were laid on the table of the board for reference. The case is, no doubt,

one of some difficulty, but the appellant has not made out to my satisfaction that the respondent wilfully (as that term is explained in the cases I have referred to) misappropriated the company's funds in payment of dividends. My Lords, what I have said is sufficient for the decision of this appeal. But I desire to express my dissent from some propositions of law which were laid down in the Court of Appeal, and upon which your Lordships thought it right to hear the respondent's counsel. The learned Judges seem to have thought that a joint stock company, incorporated under the Companies Acts, may write off to capital losses incurred in previous years, and may in any subsequent year, if the receipts for that year exceed the outgoings, pay dividends out of such excess without making up the Capital Account. If this proposition be well founded it appears to me that a company whose capital is not represented by available assets need never trouble itself to reduce its capital, with the leave of the Court and subject to the other conditions imposed by the Act of 1877, in order to enable itself to pay dividends out of current receipts. My Lords, it may be that I have misapprehended the statement of law intended to be made by learned Judges in the Court of Appeal. I think that is possible, because I find that in *Verner v. General and Commercial Investment Trust* (1894, 2 Ch. 124, at page 266). "Perhaps," Lord Lindley says, "the shortest way of expressing the distinction which I am endeavouring to explain is to say that fixed capital may be sunk or lost, and yet that the excess of current receipts over current payments may be divided, but that floating or circulating capital must be kept up, as otherwise it will enter into and form part of such excess, in which case to divide such excess without deducting the capital which forms part of it will be contrary to law." I reserve my opinion as to the effect of an actual and ascertained loss of part of the company's fixed capital, as in the case put by Mr. Swinfen Eady of a loss of a ship uninsured. But, subject to this observation, I think that the statement of law in the passage I have quoted is not open to objection, and it is only because the learned Judge appears to me to have departed from it in his judgment in the present case that I have troubled your Lordships with these remarks. I agree that the appeal should be dismissed.

Lord Brampton concurred.

(*Times*, 2 August 1901.)

The case of *BOND v. THE BARROW HÆMATITE STEEL COMPANY, LIM.*

(Decided before Mr. Justice FARWELL, in the Chancery Division, on 18th January 1902.)

Held that Preference Shareholders cannot claim to receive Dividends out of Current Profits as a matter of right, and without regard to such provision for Reserves as the Directors may think needful.

Judgment was delivered in this important action, which was before the Court last sittings. The facts and arguments sufficiently appear from the judgment.

JUDGMENT.

Mr. Justice Farwell: The defendant company were incorporated in the year 1864 with a capital of £150,000, which has since been first increased and subsequently reduced and now stands at £1,528,275, divided into 150,000 ordinary shares of £7 10s. each, 377 8 per cent. preference shares of £75 each, and 50,000 preference shares of £7 10s. each. The plaintiffs are holders of some of each of these classes of preference shares, and they claim, on behalf of themselves and all other holders of preference shares, to be paid the dividends and arrears of dividends on their shares out of the profits which they allege that the company has made in the years 1898, 1899, and 1900. No dividend has been paid on the 8 per cent. preference shares since 1898, or on the 6 per cent. preference shares since 1896. The preference shareholders have no vote in respect of these shares. The Profit and Loss Account for the year 1898 shows a balance described as "net profits for the year 1898" of £65,803 7s. 3d., and of this £20,000 was carried to Reserve Account, making it £40,000, and £10,418 10s. was carried forward. The Profit and Loss Account for the year 1899 shows a balance described as "net profit for the year 1899," of £89,018 17s. 6d., and this was carried forward pending the decision of the Court on an application for the reduction of the capital of the company, to which I will refer presently. The Profit and Loss Account for the year 1900 shows a balance of £157,605 12s. 11d., which is provisionally brought forward. The report for the year 1898 contains the following statement:—"The shareholders are aware, both from the Balance Sheets themselves and the Auditors' certificates which have accompanied them, that for some years past no depreciation has been written off the amounts at debit of Land, Buildings, Works, Fixed Plant, and Mining Leases. The directors have carefully considered the matter, and, having regard to

the fact that many of these assets are more or less of a wasting character, they are of opinion that the time has arrived when a careful revision of their value should be made. It is, however, a subject which in all its bearings requires most mature consideration, and the deliberations of the directors are not sufficiently advanced at the present time for them to submit any recommendation to the shareholders." Accordingly, in the year 1899 special resolutions were passed for the reduction of the capital of the company. The petition for the confirmation of these resolutions came before the Court in August 1900 (2 Ch. 846), and was opposed by some of the preference shareholders, and the petition was dismissed by Mr. Justice Cozens-Hardy, and his order was confirmed by the Court of Appeal (1901, 2 Ch. 746). Some, but not all, of the present plaintiffs appeared and opposed this petition, and the petition was dismissed on the ground that the alleged loss had not been proved to the satisfaction of the Court, and also by Mr. Justice Cozens-Hardy on the ground that the amount standing to the credit of the reserve fund and the £89,018 17s. 6d. profit for the year 1899 were applicable to make good loss of capital so far as they would extend. The plaintiffs in the present action are now claiming that these sums and the balance to the credit of Profit and Loss Account in 1900 are not so applicable, but belong to them by contract, and it is argued on behalf of the defendants that Mr. Justice Cozens-Hardy's order creates an estoppel, and this may possibly be correct so far as regards any of the plaintiffs who appeared and opposed the petition. But this is not pleaded, and as there are other plaintiffs who did not appear on the petition, and who could sue on behalf of themselves and all other preference shareholders who did not oppose the petition, I do not think it necessary to express any conclusive opinion on this point. Nor can I regard Mr. Justice Cozens-Hardy's decision as a precedent disposing of this case, for the points argued before me were not before him and that by no fault of the plaintiffs, because the contentions that they now raise could not have been put forward by them in support of their opposition to the petition, but were adverse to such opposition, and should, if urged at all, have been urged by the company. The contention of the plaintiffs in this action is that they are entitled by contract to be paid a preferential dividend out of the balance to the credit of the Profit and Loss Account in each year, and that the company cannot appropriate any part of such balance to reserve, or carry over one shilling until they have been paid in full. There is no suggestion of want of *bona fides* on the part of the directors or of the company. The defendants contend that this is not the true construction of the special resolutions creating the preference shares, and that, if it is, the balance to the credit of profit and loss

for any year is not necessarily such profits of the company as are properly applicable to dividend, but that if the Court is satisfied by the evidence that there have been ascertained losses and depreciations of capital assets exceeding the amount of the balances, these losses must be made good before any dividend can be paid. The first point depends on the construction of the original articles and the special resolutions creating the preference shares, for it is not contended that if the preference shareholders have such contractual rights as they claim, the company can by subsequent special resolutions deprive them of such rights or of any part thereof. Article 43 provides as follows: "Any capital raised by the creation of new shares shall be considered as part of the original capital, and shall be subject to the same provisions with reference to the payment of calls, the forfeiture of shares on non-payment of calls or otherwise, as if it had been part of the original capital, except that it shall be lawful for the company in general meeting, by special resolution as aforesaid, to direct that the new shares shall have such priority in respect of dividends as it shall deem expedient." This article, in my opinion, provides that all new shares shall be subject in all respects to all the provisions of the articles, except only that dividends payable on new shares may rank in priority to, instead of *pari passu* with, ordinary shares. For this purpose it is necessary only to introduce modifying words in Article 95, and then the whole *fasciculus* of clauses relating to dividends (95 to 101) apply. It is argued that the provisions as to the declaration of a dividend do not apply to shares on which a fixed preferential dividend is payable. In my opinion, this is not so. The necessity for the declaration of a dividend as a condition precedent to an action to recover is stated in general terms in Lindley on "Companies" (5th edition, p. 437), and, where the reserve fund article applies, it is obvious that such a declaration is essential, for the shareholder has no right to any payment until the corporate body has determined that the money can properly be paid away. It is urged that this puts the preference shareholders at the mercy of the company, but the preference shareholders came in on these terms and this argument does not carry much weight in an action such as this where *bona fides* is conceded. The opposite conclusion might enable the preference shareholders to ruin the company, and would certainly lead to great inconvenience in enabling them to compel the payment out of the last penny without carrying forward any balance. Granted that it is a hardship to go without dividends for a time, this hardship presses more heavily on the ordinary shareholders, who have to wait until the preference shareholders have received all arrears before they can get anything. It was urged that Article 97 providing for the reserve fund cannot

apply to preference shares, because one of its objects is to equalise dividends, but I cannot see that the mention of one object which is not applicable is any reason for excluding those objects which are applicable, and which are really for the benefit of all the shareholders. On the articles as they stand, I have no doubt that the true construction is that which I have stated. But it is contended that the special resolutions have created larger rights, and it was, in my opinion, competent to the company by such resolution to alter Article 43. Now the 8 per cent. preference shares are created by resolutions of 1872 in these terms:—“(1) This company will agree to purchase from the Barrow Rolling Mills Company, Lim., the two furnaces erected by that company, and the land purchased by them, and any other property of which the Rolling Mills Company may be possessed. (2) The consideration for the purchase shall be the sum of £37,700 in preference shares of this company, bearing interest at 8 per cent. per annum from the 1st of January last, such preference shares to be issued to the present shareholders in the Rolling Mills Company in proportion to their holdings. (3) The directors are authorised to issue preference shares to the amount of £37,700, bearing interest at 8 per cent. per annum in perpetuity, for the purpose of carrying out the above arrangement. (4) The holders of the above-mentioned preference shares shall be entitled to attend the general meetings of this company, but they shall not be entitled in virtue of such shares to vote, or to interfere in any way in the company's proceedings, nor shall they, in virtue of such shares be eligible as directors of the company.” In my opinion there is nothing whatever in this to alter any of the articles as I have construed them. Stress has been laid on the word “interest”; but in my opinion that word has slipped in *per incuriam*, and should be read as “dividend,” as indeed is done when this resolution is referred to in the special resolutions of 1876, to which I shall have to refer presently. Interest is not an apt word to express the return to which a shareholder is entitled in respect of shares paid up in due course and not by way of advance. Interest is compensation for delay in payment, and is not accurately applied to the share of profits of trading, although it may be used as an inaccurate mode of expressing the measure of the share of such profits. It is impossible, in my opinion, to give to the word used as it is in this case so pregnant a meaning as the plaintiffs derive, reading is as equivalent to an alteration of the articles and as creating a right overriding the valuable and possibly essential article providing for reserve funds. The 6 per cent. preference shares present more difficulty. They were created by resolutions of 1876 as follows:—“(1) The capital of the company shall be and is hereby increased by the addition thereto of 50,000 preference shares of

£10 each, entitling the holder to a fixed dividend at the rate of £6 per centum per annum on the amount for the time being paid up in respect of such shares. (3) The holders of the said new preference shares shall be entitled to a dividend thereon only after payment of the interest from time to time payable in respect of the mortgage and bond or debenture debts of the company, and after payment of a dividend at the rate of £8 per centum per annum on the preference shares of the company, amounting to £37,700 created by special resolutions passed and confirmed at extraordinary general meetings of the company in the year 1872; and in case in any year the net profits of the company shall not be sufficient for the payment in full of the dividends on such new preference shares, the net profits of any subsequent year shall (after payment thereof of interest on the mortgage bond or debenture debts of the company, and of dividends of the said £8 per cent. preference shares) be applied in payment to the holders of the said new preference shares of the amount by which the dividends of any previous year or years may have fallen short of the fixed rate of £6 per cent." The third resolution is not very happily worded, but I have come to the conclusion that this and the first resolution read together are merely a verbose statement of a bargain that the holders of the 6 per cent. shares are to have a fixed 6 per cent. cumulative preferential dividend, subject to the rights of the debenture-holders and the 8 per cent. preference shareholders. I think that the words "only after payment, &c.," in No. (3) are restrictive words, equivalent to "subject to," and do not create new rights by rescinding the articles relating to declaration of dividends, creation of reserve fund, and the like. The only difficulty that I have felt has been created by the latter part of No. (3), beginning "the net profits of any such year." I feel the difficulty of limiting the generality of the term "net profits," but, on the other hand, it is only the arrears to which this provision applies, and it would be strange that the preference shareholders should have to allow a reserve fund to be formed so far as their current year's dividend was concerned, but should be entitled to sweep up everything in respect of past arrears. I have come to the conclusion that the use of the words "net profits" is not sufficient to rescind the articles to which I have referred, but that the resolution must be read as subject to the provisions of those articles. For the reasons that I have stated the plaintiffs' case fails. But another point has been taken by the defendants, and, as evidence has been adduced and considerable argument has been addressed to it, I feel bound to state the conclusion at which I have arrived with respect to it. The construction is that, even if the plaintiffs were right in their construction of the articles, the company could not legally pay them the dividends that they claim

because there are no profits properly so called out of which they can be paid, and that any such payment, if made, would be made out of capital. It has been proved to my satisfaction (and, indeed, Mr. Jenkins very properly admitted that he could not dispute that the result of the evidence was) that the company has sustained an actual ascertained and realised loss of capital to an amount exceeding £200,000, and has also lost capital by estimate and valuation to an amount exceeding £50,000. The various sums claimed by the plaintiffs as available to pay their dividends amount to about £240,000. If, therefore, these ascertained and estimated losses have to be made good before any dividend can properly be paid, there are obviously no funds out of which to pay dividends. The defendants allege and the plaintiffs deny that the company are bound to make good these losses before paying any dividend. The question is one of very considerable difficulty on the authorities, but the result of these authorities is, in my opinion, that there is no hard and fast rule by which the Court can determine what is capital and what is profit. "The mode and manner in which a business is carried on and what is usual or the reverse may have a considerable influence in determining the question." (Per the Q.C. in *Dovey v. Cory*, 1901, A.C. 486.) "It may be safely said that what losses can be properly charged to capital and what to income is a matter for business men to determine, and it is often a matter on which the opinion of honest and competent men will differ. There is no hard and fast legal rule on the subject." (Per Lord Justice Lindley, 1899, 2 Ch. 670.) It is, however, necessary to bear in mind that the two propositions—(1) that dividends must not be paid out of capital, and (2) that dividends may only be paid out of profits—are not identical but diverse. The first is the requirement of the statutes, and cannot be dispensed with; the latter is in Table A in the articles of the particular company, and is one of the regulations of the company which has to be construed. A company which has a balance to the credit of its Profit and Loss Account is not bound at once to apply that sum in making good an estimated deficiency in value of its capital assets. It may carry it to a Suspense Account or to Reserve, and if the assets subsequently increase in value the amount neither has been nor will be part of the capital. If, therefore, a part of such balance is used in paying dividends, such dividend is not paid out of capital, because the sum has never become capital, although it still remains a question whether it has been paid out of profits or not. It has been pointed out by Lord Justice Lindley in *Lee v. Neuchâtel Asphalte Company* (41 Ch.D. 1), that there is nothing in the statutes requiring the company to keep up the value of its capital assets to the level of its nominal capital. The requirement is merely negative, that

dividends shall not be paid out of capital, and the balance to the credit of Profit and Loss Account does not automatically become part of the capital assets because the value of the actual capital assets has depreciated to an amount equal to or exceeding such balance. The real question for determination, therefore, is whether there are profits available for distribution, and this is to be answered according to the circumstances of each particular case, the nature of the company, and the evidence of competent witnesses. There is no single definition of the word "profits" which will fit all cases. Take, for instance, Professor Marshall's definition ("Economics," Edn. of 1883, p. 142):—"The excess of the receipts from the business during the year over the outlay for the business, the difference between the value of the stock and plant at the end and at the beginning of the year being taken as part of the receipts or as part of the outlay according as there has been an increase or decrease of value." I am precluded from adopting this in its entirety by authorities which are binding on me, because in the definition "stock and plant" obviously include both fixed and circulating capital as defined at p. 134 of the same treatise. See, for instance, Lord Lindley's judgment in *Verner's case* (1894, 2 Ch., at p. 266), where he says:—"Perhaps the shortest way of expressing the distinction which I am endeavouring to explain is to say that fixed capital may be sunk and lost, and yet that the excess of current receipts over current payments may be divided, but that floating or circulating capital must be kept up." I do not understand his Lordship to be laying down a general and universal rule that in every company fixed capital may be sunk and lost, but that there are companies in which that may be the case. All the authorities, however, agree, I think, that circulating capital must be kept up. Now in the present case the £200,000 realised loss arises by the surrender of the leases of certain mines, by the pulling down of certain furnaces, and on the sale of certain cottages. The company is a smelting company on a very large scale, and for the convenience of its works and by way of economy they acquired the leases of the surrendered mines in order to supply themselves with their own ore instead of buying it as required. The ore was used exclusively for the purposes of the company's works. The mines were drowned out and the cost of pumping them out was prohibitive. The company, therefore, surrendered the leases, pulled down the blast furnaces, and sold the cottages connected therewith. Now the evidence before me is all on one side. The plaintiffs called none, and Sir David Dale and the defendants' other witnesses all agree that in a company of this nature these items ought to come into the account before any profit can be said to be earned, and my own opinion coincides with theirs, inasmuch as I think that the money invested in

those items is properly regarded in this company as circulating capital. Suppose the company had bought enormous stocks of ore sufficient to last for ten years, it could hardly be said that the true value of so much of this as remained from time to time ought not to be brought into the Balance Sheet, and I can see no difference for the purpose of the account between ore *in situ* and ore so bought in advance. The blast furnaces and cottages are mere accessories to the ore, and resemble a building for burning the stores bought in advance already mentioned. There is more difficulty about the remaining £50,000. I think that the onus is on the plaintiff to show that it is fixed capital and that in a company of this nature such fixed capital may be sunk or lost. They have not done this, and the evidence, so far as it goes, is the other way. But this is not an actual loss, but depreciation by estimate. The plaintiffs really relied on *Lee v. Neuchâtel Asphalte Company* as an authority for this proposition as a universal negative—viz., “that no company owning wasting property need ever create a depreciation fund.” In my opinion that is not the true result of the decision. It must be remembered that in that case there had been no loss of assets. The company’s assets were larger than at its formation (see p. 15), and the Court decided nothing more than the particular proposition that some companies with wasting assets need have no depreciation fund. For instance, I cannot think that it would be right for the defendant company to purchase out of capital the last two or three years of a valuable patent and distribute the whole of the receipts in respect thereof as profits without replacing the capital expended in purchase. It is for the Court to determine in each case on evidence whether the particular company ought, or ought not, to have such a fund. There is no doubt as to the opinion of the witnesses in this case, and, further, the opinion of the directors cannot be altogether disregarded. The Courts have, no doubt in many cases, overruled directors who proposed to pay dividends, but I am not aware of any case in which the Court has compelled them to pay when they have expressed their opinion that the state of the accounts do not admit of any such payment. In a matter depending on evidence and expert opinion it would be a very strong measure for the Court to override the directors in such a manner. I have made no distinction between the realised loss and the estimated loss, because the witnesses declined to recognise any such distinction, and also because the decided cases deal only with the distinction between floating and fixed capital, and do not distinguish between realised and estimated loss, and it would serve no useful purpose for me to express any opinion on the subject. The result is that the action fails, and must be dismissed with costs.

(Times, 17 January 1902.)

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The case of **BELLERBY v. ROWLAND AND MARWOOD'S
STEAMSHIP COMPANY, LIM.**

(Decided before COLLINS, M.R., STIRLING, and COZENS-HARDY, L.JJ.,
in the Court of Appeal, on 6th May 1902.)

*Held that a Surrender of partly paid-up Shares to a Company, to cover Losses
incurred, is invalid.*

This was an appeal against the decision of Mr. Justice Kekewich, reported 27 *Acct.* L.R. 90. A question of general importance was raised as to the power of a company to accept a surrender of shares. The action was brought to test the validity of a surrender of 415 shares in the defendant company made in the year 1893 in favour of the company by the then directors—viz., Messrs. Bellerby, Moss, Marwood, Wright, and Rowland. The action was brought by the three first-named directors and the executors of the two others, who had since died. The company was incorporated in the year 1890 under the Companies Acts with a capital of £275,000, divided into 25,000 shares of £11 each, for the purpose of carrying on the business of shipowners. By Article 37 of the company's articles of association it was provided that "the directors may accept from any member, on such terms and conditions as shall be agreed, the surrender of his shares or stock, or any part thereof." The circumstances which led to the surrender were as follows:—In 1893 the company gave an order to certain contractors for a new steamship called the "Golden Cross." Owing to the depressed condition of the shipping trade at that time it was difficult to provide the necessary funds for the payment of the contractors, and the ship was sold by the company to the International Line Steamship Company during her first voyage in order to pay the contractors. The result of the sale was that the company incurred a loss of £4,000 in respect of the contract. The directors, with a view to relieving the company from loss, but without admitting any liability in respect of the loss, agreed that each should surrender to the company 33 shares, which were then paid up to the extent of £10 only; and by a deed poll executed in July 1893 they formally surrendered the shares in question, their object being (as therein stated) to make good to the company all losses sustained by it in relation to the steamship "Golden Cross" recently sold by them as such directors to the International Line Steamship Company. Since 1893 the company had prospered, and it was suggested that some special remuneration should be made to the directors, and that this should take the form of a return to them of the shares which they had surrendered. At a meeting of the shareholders held on October 10th 1900 this course was unanimously approved, and it was resolved that a friendly action

should be brought for the purpose of obtaining the opinion of the Court as to the validity of the surrender, having regard to the fact that the directors were advised that the only way in which a return of the shares could be effectually made to them was by having the purported surrender set aside. The plaintiffs accordingly brought this action, claiming a declaration that the surrender was *ultra vires* and inoperative, and to have their names restored to the register in respect of the 415 shares. Mr. Justice Kekewich held that the surrender of the shares was really a purchase of them by the company, the price given being the release of the directors from the liability of £1 per share. The transaction was therefore void, it being conclusively settled by the decision of the House of Lords in *Trevor v. Whitworth* (12 App. Cas., 409) that a company cannot purchase its own shares. But, after the length of time which had elapsed since the transaction took place, his Lordship was of opinion that it would not be equitable to admit the claim of the plaintiffs to be restored to the register merely because the company had now become much more prosperous. His Lordship accordingly dismissed the action. The plaintiffs appealed.

The appeal was heard on April 18th 1902, when the judgment of the Court was reserved.

JUDGMENT.

The Court allowed the appeal.

The Master of the Rolls, after stating the facts, read his judgment as follows:—Since the case of *Trevor v. Whitworth* (12 App. Cas. 409) it is clear law that a limited company incorporated under the Joint Stock Companies Acts cannot purchase its own shares unless it does so by way of reduction of capital with the sanction of the Court under the provisions of the Companies Acts of 1867 and 1877. See *British and American, &c., Corporation v. Cowper* (1894 A.C. 399). Cases dealing with the acquisition by companies of their own shares before *Trevor v. Whitworth* was decided are now of little assistance. Is, then, the transaction in this case a purchase by the company of its own shares? It was certainly intended by the parties who carried it out to involve the release by the company to the surrenderors of the right to call up the unpaid balance of £1 on each share, and was therefore not a gratuitous surrender. There was an exchange of real consideration between the parties, and therefore it ought to be described perhaps more accurately as a sale and purchase than as a surrender. But assuming it can be properly described as a surrender, although it involves a consideration given out of the assets of the company to the party surrendering, it remains to consider whether there is any legal

ground upon which it can be taken out of the principle of *Trevor v. Whitworth*. It seems to me that there is not. An argument was addressed to us by Mr. Warrington based on a minute criticism of some passages in the speeches of the learned Lords in which they deal with the argument that to hold a sale bad would be to forbid forfeitures and surrenders, and point out that these differ from the case actually before them, which involved a present parting by the company with the amount actually paid-up on the shares. But, whether this distinction is conclusive or not, it seems to me that when closely criticised these *dicta* as to surrenders deal with them as a species of forfeiture, which, as the learned Lords point out, is recognised by the Act itself, and cannot be extended to cover a transaction having none of the elements of a forfeiture. [His Lordship then read passages from the speeches of Lord Herschell in *Trevor v. Whitworth* (12 App. Cas., at p. 417), of Lord Watson in the same case (at p. 429), and of Lord Macnaghten in the same case (at p. 438), as showing that "a surrender of shares in return for money paid by the company is a sale, and open to the same objections as a sale." His Lordship also referred to a passage in the speech of Lord Macnaghten in *British and American Corporation v. Cowper* (1894 App. Cas., at p. 414) to a similar effect.] I can see no distinction in principle between returning to a shareholder a part of the paid-up capital in exchange for his shares and wiping out his liability for the uncalled-up sum payable thereon. Both methods involve a reduction of the capital which, as Lord Watson points out in *Trevor v. Whitworth* (at p. 423), persons dealing with the company are entitled to rely upon as existing either as paid up or as still to be called up, and such a reduction, therefore, can only hold good if sanctioned under the conditions prescribed. If it be objected that the shares may, in the language of Lord Watson, be "reissued," and that though the liability of the surrenderor to pay the amount still at call is extinguished, the liability will remain good against anyone to whom the company disposes of the share, the answer in this case is the same as that suggested by Lord Watson in the case where the money paid up on the share is returned to the shareholder. He says, at p. 424, "In the event of the company continuing to hold the shares (as in the present case) the amount paid up is permanently withdrawn from its trading capital." But further, and apart from the question of sale or trafficking in a company's own shares, I think the reasoning in *Ooregum Gold Mining Company of India v. Roper* (1892, A.C. 125) establishes that to release a shareholder from any part of his obligation to pay the uncalled-up balance on his share is an *ultra vires* act on the part of the company. "It seems to me," says Lord Halsbury (at p. 133), "that the system thus created by which the shareholder's

liability is to be limited by the amount unpaid upon his shares renders it impossible for the company to depart from that requirement, and by any expedient to arrange with their shareholders that they shall not be liable for the amount unpaid on the shares, although the amount of those shares has been, in accordance with the Act of Parliament, fixed at a certain sum of money. It is manifest that if the company could do so the provision in question would operate nothing. I observe in the argument it has been sought to draw a distinction between the nominal capital and the capital which is assumed to be the real capital. I can find no authority for such a distinction. The capital is fixed and certain, and every creditor of the company is entitled to look to that capital as his security"; and the opinions of the other learned Lords are to the same effect. The justification of forfeitures rests upon the statute itself, and I think that since *Trevor v. Whitworth* no authority can be relied on as justifying a surrender having the effect of reducing capital which cannot be supported as a form of forfeiture. It is not necessary to refer to *Eichbaum v. City of Chicago, &c., Company* (1891, 3 Ch. 459), decided by my brother Stirling on the authority of *Ex parte Teasdale* (L.R. 9 Ch. 54), as he will deal with those cases himself. In *In re Denver Hotel Company* (1893, 1 Ch. 495), Lord Justice Lindley, in supporting a surrender, relied on the fact, pressed by counsel in argument, that "the shares being fully paid up, their surrender involved no release by the company of any of its rights against the surrenderor," indicating thereby the possible importance of a release. It is not, however, necessary to consider in this case whether a surrender, even of fully paid-up shares, could be supported. I am of opinion, therefore, that Mr. Justice Kekewich was right in his decision on the principal question in the case. Upon the second point, however, Mr. Justice Kekewich has held that, notwithstanding that the surrender of the shares was void as being an act *ultra vires*, still the application to restore the plaintiffs to the register must be treated as being made under Section 35 of the Act of 1862, and that he was not satisfied of the justice of the case within that section, and he therefore refused to make the order. The learned Judge relied on the fact that so much time had elapsed since the surrender, and that it was conceivable that some persons might have altered their position on the footing that the capital of the company had been reduced, and, relying upon *Sichell's* case and the *dicta* of Lord Macnaghten in *Trevor v. Whitworth*, he held that the plaintiffs showed no equity in their favour to disturb the existing state of things, and therefore refused to rectify the register at their instance. The application in this case is not in fact made under Section 35 (if anything turns upon that), but is an action, asserting the legal right in the plaintiffs to be on the register,

on the ground that the act whereby they were removed from it was *ultra vires*, and therefore a nullity. *Sichell's* case did not relate to an act *ultra vires* of the company, and in Lord Macnaghten's observations in *Trevor v. Whitworth* on *In re Dronfield Silkstone Coal Company* he treated the application as made by one who had no equity to set the Court in motion. Here it seems to me that in point of law the plaintiffs never ceased to be the legal owners of the shares, and therefore are not obliged to rely upon an equity to have the register rectified. Nor, on the other hand, can the company set up lapse of time or acquiescence as validating that which was in its essence incapable of being made valid, being, as Sir G. Jessel, Master of the Rolls, pointed out in the *Dronfield* case, void and not voidable only. The Scotch case, *General Property Investment Company and Matheson's Trustees* (Court of Session Cases, 4th Series, Vol. 16, p. 282), is an authority directly in point on this part of the case, unless the fact of liquidation makes a difference. An action was there brought by the liquidator to place on the register a shareholder who had sold his share to the company at their instance many years before, and Lord Shand, in dealing with an argument based on Section 35, said (at p. 291), "If the legal right of the company be clear, then it follows that the justice of the case requires that effect shall be given to that right." It seems to me, therefore, that the learned Judge's decision on this part of the case cannot be supported, and that the appeal must be allowed.

Lord Justice Stirling read a judgment, in which he said that he had arrived at the same conclusion on both points, though not without some doubt upon the first.

Lord Justice Cozens-Hardy read a judgment to the same effect.

(*Times*, 5 May 1902.)

The case of HILDER AND OTHERS v. DEXTER.

(Decided before Lords HALSBURY, DAVEY, ROBERTSON, and BRAMPTON, in the House of Lords, on August 5th 1902.)

Held that an Option given to Underwriters to subscribe for Shares at par at a future date is not contrary to the provisions of Section 8 of the Companies Act, 1900.

The following statement of facts is taken in substance from the judgments of Lord Davey and Lord Brampton.

The United Gold Coast Mining Properties, Lim., was incorporated on December 17 1900, with a capital of £200,000, divided into 200,000 shares of £1 each. In January 1901 the directors determined to issue

33,333 shares, or one-sixth of their nominal capital. They did so by offering the shares, not to the public, but to 14 persons, of whom the appellant Hilder was one, and who were invited to apply for the shares. Hilder applied for and was allotted 6,975 shares upon the following terms:—

“For each share allotted in accordance with this application a subscriber shall have the option during the period of one year from the 3rd of January 1901 of taking up at par a further ordinary share of £1 in the initial capital of the company, and in the event of such last-mentioned share being taken up under such option, a further option during the two years from and after the said third day of January 1901 of taking up at par a further ordinary share of £1 in the initial capital of the company.”

For these shares Hilder paid £6,975. The rest of the 33,333 shares were allotted upon the same terms to the other 13 applicants. In July 1901 the £1 shares were selling at about £2 17s. 6d., and Hilder gave the company notice that he elected to take the further shares under his agreement with the company. The respondent, a shareholder, having brought an action against Hilder, the company, and the directors, Byrne, J., holding the case governed by *Burrows v. Matabele Gold Reefs and Estates Co., Lim.*, granted an injunction restraining the company and directors from carrying out the agreement. This decision was affirmed by the Court of Appeal (Rigby, Collins, and Romer, L.JJ., on the same ground, but reversed by the House of Lords for the reasons stated below:—

Lord Davey (after stating the facts given above, and the mode of issuing the 33,333 shares) said: My Lords, There is nothing whatever in the case to throw doubt upon the good faith of the directors in selecting this mode of issuing the shares of the company, in preference to offering them for public subscription in the ordinary way, or to impeach their exercise of the discretion vested in them by the articles. It appears from the affidavits that the scheme was to raise the necessary working capital by the issue of one-half of the share capital for cash, the other half being used for the purpose of payment in shares credited as fully paid-up for the concessions to be purchased by the company. But it was said that this mode of raising the sum required for working capital is prohibited by Section 8, Sub-section 2, of the recent Act of 1900, and is therefore beyond the power of the company.

Now, before construing the words of the section which is relied upon, your Lordships are entitled to consider the state of the law before the section was passed, with a view to ascertaining the mischief to which

the enactment is directed. It was decided by this House in *Ooregum v. Roper* that a stipulation or agreement that a less cash sum than the nominal amount of the share shall be accepted as payment for the share is repugnant and void. On the other hand, there was authority for saying that the payment of a commission to brokers or others who undertook to procure subscriptions, or in default to subscribe for a certain number of shares, was legitimate. That doctrine, however, did not meet with universal acceptance, although it had the support of Buckley, J., in his valuable work on the Companies Acts. It was thought by some that such a payment when made out of capital was a misapplication of the company's capital, and was therefore *ultra vires*. There were, therefore, two points for consideration: first, that shares could not be issued at a discount, *i.e.*, subject to an agreement that the applicant should pay less to the company than the nominal value of the share; and, secondly, the question whether the payment, out of capital moneys or by means of shares credited as fully or partly paid-up, of what is called an underwriting commission was within the powers of the company.

From a perusal of the 8th Section of the Act of 1900 your Lordships will infer that the Legislature was desirous of enabling remuneration to be paid for services rendered in placing or procuring subscriptions of the company's capital, and it appears to have hit upon what may be termed a compromise. By the first sub-section a company is empowered, upon any offer of shares to the public for subscription, to pay a commission to any person in consideration of his subscribing or agreeing to subscribe, whether absolutely or conditionally, for any shares in the company, or procuring or agreeing to procure subscriptions, whether absolute or conditional, for any shares in the company, subject to certain defined conditions as to amount and disclosure. This sub-section, however, permits a limited application of the company's capital in payment of a commission. Then follows the second sub-section, on which the question before your Lordships turns. It is in the following terms: "Save as aforesaid no company shall apply any of its shares either directly or indirectly in payment of a commission, discount, or allowance to any person in consideration of his subscribing or agreeing to subscribe, whether absolutely or conditionally, for any shares in the company, whether the share or money be so applied by being added to the purchase-money, or in property acquired by the company, or to the contract price of the work to be executed for the company, or the money be paid out of the nominal purchase-money or contract price or otherwise." And the third sub-section provides that nothing in this action shall affect the power of any company to pay such brokerage as it has hitherto been lawful for a company to pay.

The first words to be construed are, "apply any of its shares or capital money." I think that these words naturally mean—apply its capital, either in the form of shares before issue when they may be described as potential capital, or in the form of money derived from the issuing of its shares. "In payment of any commission, discount, or allowance": I think this means payment by the company. The words "discount or allowance" seem to mean the same thing—namely, a rebate on what would justly be due from the subscriber on such shares. The advantage which the appellant will derive from the exercise of his option is certainly not a "discount or allowance," because he will have to pay 20s. in the £ for every share. Nor is it, in my opinion, a commission paid by the company, for the company will not part with any portion of its capital which is received by it intact, or indeed with any moneys belonging to it. But the words relied on are "either directly or indirectly," and the argument seems to be that the company, by engaging to allot shares at par to the shareholder at a future date, is applying or using its shares in such a manner as to give him a possible benefit at the expense of the company in this sense, that it foregoes the chance of issuing them at a premium. With regard to the latter point, it may or may not be at the expense of the company. I am not aware of any law which obliges a company to issue its shares above par because they are saleable at a premium in the market. It depends upon the circumstances of each case whether it will be prudent, or even possible, to do so, and it is a question for the directors to decide. But the point which, in my opinion, is alone material for the present purpose is that the benefit to the shareholder from being able to sell his shares at a premium is not obtained by him at the expense of the company's capital. The prohibited application of the shares may be direct by allotting them as fully or partly paid-up to the person underwriting the shares, or by allotting them in some other way with the intention that they shall ultimately find their way to such person or be applied in payment of his commission.

My Lords, it may be that in some particular case a contract such as that which your Lordships have before you would be open to impeachment as imprudent, or an abuse, or in excess of the powers of management committed to the directors. In this case the question is as to the powers of the company itself, and not as to the due exercise of the directors' powers. I have come to the conclusion, from a consideration of the language of Section 8, Sub-section 2, that the prohibition therein contained extends only to the application, direct or indirect, of the company's capital in payment of a commission by the company, and the transaction impeached in this case is not within it. It is satisfactory to find that the conclusion to which I have come will

not have the effect of extending the prohibition to transactions which were legitimate before the Act, and not, so far as I am aware, open to objection on any other ground.

I am of opinion that the appeal should be allowed. I move your Lordships, therefore, that the order appealed from be reversed, and that the respondent be ordered to pay to the appellants the costs both here and below.

Earl Halsbury, L.C., and Lord Robertson concurred.

Lord Brampton read a lengthy judgment to the same effect, concluding as follows:—

It is not contended that the contract would have been illegal before the Act of 1900, and I do not think it is, so far as regards the question before us, affected by that Act.

It seems to me to have been a very reasonable and prudent contract to make when it was entered into, and in carrying it out the company will have raised, without deduction of any kind, the whole of their authorised share capital of £200,000, as contemplated on its incorporation; the shares they deliver will be applied, not in payment of commission, but purely in fulfilment of the agreement of the directors for good consideration to allot them to Mr. Hilder, who will pay for them the price fixed when the contract was made.

I do not think *Burrows'* case (if rightly decided) is applicable to the present. It is materially distinguishable in this, that there the 15,000 shares in question were expressly agreed to be allotted at a price below the then market premium value in order to satisfy an agreed commission.

I think, for the reasons I have expressed, this appeal should be allowed, with costs.

Orders of the Court of Appeal and Byrne, J., reversed, with costs here and below.

(Condensed from "Law Reports.")

The case of BADHAM v. WILLIAMS.

(Decided before Mr. Justice KEKEWICH, in the Chancery Division, on
January 14 1902.)

*Held that the "Net Profits" of a Solicitor are the excess of his Cash Receipts in
respect of Costs, &c., over his Business Expenses.*

By a partnership agreement, dated the 22nd July 1880, made between Mr. G. Badham and Mr. E. W. Williams, solicitors, it was (*inter alia*) agreed as follows:—

"1. Mr. Williams is to receive £300 per annum up to the end of the year 1880, £350 per annum for the following two years. From the 1st January 1885 (in lieu thereof) Mr. Williams is to receive one-fourth of the profits (if the business shall have realised a net profit of not less than £1,600 per annum in the meantime) for the next five years, and after that one-third of the profits."

This partnership was dissolved in August 1899.

It appeared that no division of the profits had ever been made, and in taking the Partnership Accounts the question was raised whether the actual receipts and payments for each year were to be taken for the purpose of ascertaining the profits of the firm for that year, or whether moneys received subsequently to the year 1885 for work done previous to that year, when Mr. Williams first commenced to be entitled to a fixed share of the profits, should be considered as belonging to Mr. Badham, and not as profits of the firm.

This was a summons taken out by Mr. Badham for the decision of the above question.

Renshaw, K.C., and Stewart Smith for Mr. Badham: Mr. Williams was only a salaried partner before the year 1885. He ought not to be entitled to share in profits made in previous years in addition to having drawn his fixed salaries in those years.

JUDGMENT.

Kekewich, J.: This is a short question to be shortly disposed of, but it is one of considerable importance. Mr. Renshaw has just now put it in the very strongest possible way. He says draw the line at the end of the year 1884, and start entirely afresh—that is to say, treat it as a new partnership commencing from the 1st January 1885, and then as to what would have been done by Mr. Badham in 1884 the profits arising from that must belong to Mr. Badham. That is so according to my view. That must be so; but the fallacy is that it is not a new partnership. The partnership commenced many years before then, and what we are

dealing with is merely a rearrangement of the division of profits from the 1st January 1885, when Mr. Williams receives his one-fourth share of the profits. It could not be contended that he was then still a mere salaried partner. I daresay it would be put so by Mr. Badham, whether any profits were earned or not; but even if that were the proper construction of the agreement, what he is to receive at the end of the year from Mr. Badham is a certain amount. It is a partnership commencing with the written agreement and continuing into 1885. If I could adopt the view which Mr. Renshaw has put before me on behalf of the plaintiff, that you should draw the line entirely at that date and start afresh, not only should I take a different view from what I now take, but I should take it from the very reasons which urge me to take the view which I am about to express. It is quite true that a solicitor's business differs from the business of any trading concern. It is a business which we need not describe, and which we all know stands quite alone. But for the division of profits a solicitor's business must be regarded just as any other business concern, and it must stand on the same lines (so it seems to me) as any ordinary trade or business. There are no doubt many ways of testing it. You may test it with regard to the returns made for income-tax, or you may test it for the purpose of division of profits between partners, and you may test it in many ways. But one must not decide too hastily, and consider the returns of income-tax, because those are governed by law independent of the partners, whereas the division of profits between themselves is a matter entirely of agreement between the partners, and if they please they can consider as profit made in any given year profit which is not really attributable to that year. Take the hypothetical case of the first year of a partnership, which, of course, cannot, as a rule, be a profitable one in the sense that there is something coming in representing profit in that year. The system of credit which prevails in all businesses and trades prevents the possibility of a large proportion of profit being made in the first year of any concern. Supposing at the end of the first year the two partners, whether solicitors or traders, say: "We have had a very good year, we have not got much money at the bank, but it is coming in, and most of it will come in in the next three months—there is no reason why we should not divide as profits a considerable sum, and, in order to divide it as profits, why should not we draw upon our bankers?" There is nothing dishonest in that, and nothing contrary to ordinary commercial morality, and certainly nothing contrary to ordinary commercial practice. A man might consider that he was fairly entitled to divide profits and put into his own pocket a sum formed upon an estimate of business done—the money coming from the business done in year first closed. But would that be properly the profits of the year? It seems to

me that in the absence of special agreement the profits of the year must necessarily be the receipts of that given year after the expenditure and whatever else in the way of depreciation fund and so on applicable to the particular case is set against it. In the absence of a special agreement, I do not see how any accounts could otherwise properly be taken on a real footing, and, in the absence of special agreement, I venture to say that no accountant would audit accounts so as to show a profit on that mere footing; you may provide by estimate for it, but, of course, that requires, to my thinking, a special agreement. If you have no provision for an estimate, then you must take the actual facts. What is true of a trading concern is true of businesses which are not business institutions. Take haphazard such an institution as the Zoological Society of London, which, of course, cannot earn profit. Would it be possible for them to make out an account for the year 1901 on the footing that many subscribers had failed to pay, and that therefore the moneys which they ought to have paid in 1901 should be treated as receipts for that year? The total assets which you might have made you may estimate, but you cannot treat as received for the purposes of ascertaining the balance due, moneys which ought to have been paid in 1901, but which have not been paid. Although in the example I have taken there could be no question of profits, yet the same principle applies to the accounts here in the absence of special agreement. There are several cases of recent date in which the question has arisen of what a company ought to divide as profits, and that is because there is a power which sometimes exists or generally exists to estimate the profits earned for the purposes of giving the shareholders immediately a proportion of that which, according to a fair estimate, would otherwise come into the accounts of the next year. There have been many learned discussions lately and I suppose there are likely to be more, as to what may fairly be brought into account in that way for the purpose of division of profits, but, in the absence of anything of that kind, if it is a mere question what were the profits made in a particular year, it seems to me that the duty is to ascertain what cash has been received and what cash has been expended, and, if that is fairly done, you know the profits of the year. If there is a large outstanding liability which cannot be settled, the partners will estimate that, and it will not be considered as part of the profits. If there is a large outstanding possible loss, and there is a large sum due to a client, then you would provide for that. But in ascertaining what is really actually divisible for the year fairly, you take the Cash Account as it stands, and really that is the principle, of course, of income-tax returns. The income-tax return is a return of the actual receipts, less such expenditure as is properly chargeable against those receipts. Putting it in a concrete

sense, you may ask a man whether he has had a good year. He says, "Yes, I have had an excellent year, but unfortunately those with whom I have been dealing have not paid up, and consequently I find a little difficulty in meeting my Christmas bills." But that does not prevent your having had a good year in the sense of having done a large amount of business. But, of course, it makes a great deal of difference if you consider it with a view to the money he has available, and if he is asked what he has to divide he would be bound to say: "I have very little to divide. I have very little wherewith to pay, but next year I have every reason to hope from the business done that it will be better." Now, taking another example. A merchant in London consigns a cargo to some foreign port for sale in 1901. Suppose the payment is made by bills perhaps at six or three months, it may run into 1902. Now, are they to treat that as concluded in 1901, and consider that business as attributable entirely to 1901 when the bills may not be met at maturity? Are they to consider those as so much cash for the purposes of that business? It seems to me that that would be entirely wrong in the absence of a special agreement. For the purposes of the Balance Sheet, no doubt, they would estimate that there is an outstanding asset which they hope to realise; but for the purpose of ascertaining the profit and loss—that is to say, what is to be divided—it seems to me that they must consider only what they have received, because those bills will only come in when met at maturity in 1902. I am bound to consider this simply apart from any special agreement, because here all I have is that Mr. Williams is to receive a fourth part of the profits and nothing more. Is there any special agreement about that in the plaintiff's favour? There is certainly none. I do not think myself there is anything on the evidence to show that a special agreement establishing the practice would help the defendant. There is certainly nothing to help the plaintiff. That fact being so, I must decide the question quite apart from any practice which prevails, supposing practice could affect it. It seems to me on that, that although I quite see that it introduces difficulties, and that a line has to be drawn for certain purposes, and that the result of drawing that line in the way I do gives Mr. Williams a share of the profits in the business really transacted by Mr. Badham alone, he being the only responsible partner in the firm, nevertheless, treating it as a partnership which commenced as it did from the date of the written agreement, I think the general principle must apply. I shall give directions to the Master that in taking the accounts he must consider the sums received and the sums expended in each year only for the purpose of ascertaining the profits of that year.

BOALER V. THE WATCHMAKERS' ALLIANCE AND ERNEST 799
GOODE'S STORES, LIM., AND OTHERS.

The case of BOALER v. THE WATCHMAKERS' ALLIANCE AND
ERNEST GOODE'S STORES, LIM., AND OTHERS.

(Decided before Mr. Justice SWINFEN-EADY, in the Chancery Division,
on January 28 1903.)

*Held that the responsibility of Directors for Dividends improperly paid out of
Capital ceases when the deficit has been made good out of subsequent Profits.*

This was an action brought by the plaintiff, Bernard Boaler, suing on behalf of himself and all other holders of ordinary shares in the company, against the company and its directors. There were various other cross-actions and motions which were heard by his Lordship at the same time. The general nature of the case, and of the facts upon which it was based, may be gathered from the following

JUDGMENT.

His Lordship said the first case was that of *Boaler v. The Watchmakers' Alliance and others*. In this action Bernard Boaler was the plaintiff, and sued on behalf of himself and the other shareholders of the company, other than the defendants Cochrane, David, Rooker, Miller, and Oldfield. Plaintiff sought to establish that the allotment and issue of a block of shares was *ultra vires*, and asked for a rectification of the register. In the claim 27,500 were mentioned; but in the opening of the case the number was reduced to 13,208. Plaintiff also sought a declaration with regard to two sums of £42,000 and £15,000; but this was treated as struck out. Plaintiff also sought a declaration that dividends paid in 1897 and 1898 were improperly paid out of capital, and that the defendants should repay the amount to the company, and for a general injunction to restrain further dividends out of capital. The action was really divisible into two branches—one a claim in respect to the issue of 13,000 odd shares, alleged to be *ultra vires*; and the other with regard to alleged improper payment of dividend out of capital. The plaintiff, Boaler, acquired 20 preference shares and 40 ordinary shares in the company on May 27 1902, and the writ was issued in the action on June 23. He acquired the shares from Leslie Morse, against whom Cochrane had obtained judgment. Therefore, within four weeks of plaintiff acquiring the shares the writ in the action was issued, and a claim made in respect of matters which occurred long anterior to the plaintiff becoming a shareholder. Plaintiff had not given any evidence himself, though making allegations against the other defendants, and specially against Cochrane, alleging vociferously that Cochrane was afraid to go into the box. But in the result Cochrane had been examined, and the plaintiff had not gone into

the box. He (the Judge) was quite satisfied that plaintiff Boaler had no merits whatever. It was a purely technical case. The transaction on which plaintiff based his claim was recorded in the minutes as follows:—"Cochrane reported that a friend of his had purchased 27,500 ordinary shares, and as the cheque for the amount was large he had brought it personally. The shares were allotted to E. Lyons. Cochrane then said he would be glad of some ready money as part payment of the business, and asked that this cheque should be paid to his credit, to which the directors agreed."

Plaintiff's allegation was that with regard to 13,000 of the shares, plaintiff said they were unpaid, and that the issue of them by the directors was *ultra vires*. He tried to make it out by calling Mr. Lyons, who produced the cheque in question, and said it was never presented for payment and never cashed. Lyons said he was approached by letter by Cochrane, who said he wanted to take up 27,500 shares in the company, but did not want his name to appear, and asked if Lyons would apply for them, Cochrane promising to indemnify Lyons for the cost. Lyons said he bought the shares, and transferred some of them at Cochrane's request, leaving a balance of some 12,373. Those he transferred to Cochrane, which concluded the transaction. Lyons said he also accounted for the dividend to the persons interested. He said: "I refused to become a shareholder except on Mr. Cochrane's indemnity." That was all the evidence called by plaintiff. Defendant called Colonel Haddon and Mr. J. David. They said they knew Mr. Lyons as Mr. O.—a firm which had large dealings in the trade—and they looked on the cheque as a *bonâ fide* one, and that it was a good transaction for the company, as they had to pay 6 per cent. on the unpaid purchase-money. Colonel Haddon said he had no reason to doubt that Lyons' cheque was cashed, and that he was not in the least suspicious that it was not a *bonâ fide* transaction. He also said the agreement between Cochrane and the company was sealed on June 29. The result of that was that there was an agreement for the sale of the business of the company duly entered into and sealed. It was, no doubt, in existence, though it seemed to have been mislaid. At the date of the allotment to Lyons of the shares (July 8) there was a subsisting contract between the vendor and the company, under which the company were liable to pay the purchase-money for the business. There was also an application for 27,500 shares, which the directors *bonâ fide* believed to be in order, and at the same time the vendor offered to take the cheque for the shares in part payment of the purchase-money. That was to the relief of the company, as it saved them 6 per cent. interest. He entirely accepted what Colonel Haddon and Mr. David had said, and on that footing he was of opinion that the shares allotted to Lyons

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were to be treated, and must be accepted, as fully paid. It was wholly inaccurate to say that the company received no value for the 27,500 shares, and it was idle to suggest that. That was sufficient to show that the plaintiff, endeavouring to question a transaction which took place years before he joined the company, on a technical ground, failed on the technicality, and that alone would be sufficient to dispose of the action on that ground. Therefore the plaintiff's claim that the shares allotted to Lyons were allotted *ultra vires* was misconceived, and wholly failed.

He next claimed that dividend was paid out of capital. The Profit and Loss Accounts had been regularly made out by qualified persons, and plaintiff had adduced no evidence to show the accounts were irregular or improper; but he sought to make out his case by reference to two sums of £7,000 and £10,000. In the first year of working there was an interim dividend paid out of net profits, and there was a reserve of £7,000, which was obtained by considering the business as worth £92,000, when only £85,000 was paid for it. He was of opinion that this was improper, and ought not to have been done, and if dividend had been paid out of it and had not been restored, the plaintiff would have been right in his action. But plaintiff had ignored the material fact that Mr. Dicksee (one of the auditors) required this money to be written back and the amount used for dividend restored, and this had been done. He was therefore of opinion that plaintiff had shown no ground for saying that dividends had been improperly paid out of capital. The other question was with regard to 10,000 shares transferred from Cochrane to three other directors, and plaintiff contended that was an irregular arrangement. But that was a fallacy. The purchase-price standing at £85,000, Cochrane was willing to assist the directors by reducing it £10,000, and he did this by surrendering 10,000 shares to the directors, which stood for the time in the directors' names. Mr. Boaler suggested, without a tittle of evidence, that this £10,000 was not represented by available assets. That was an idle suggestion, and so far as the evidence was concerned it was the other way, the business being fully worth the price paid for it. Plaintiff further suggested there was no net profit, as no allowance had been made for depreciation; but he did not prove there was any depreciation to provide for. The evidence was, in fact, the other way. The result was that in so far as plaintiff claimed a declaration the dividends had been paid out of capital, it had been established before the Court that the dividends were paid out of profits, and that the £7,000 item, on which the claim was based, had been written back. There was nothing in the item of £10,000. The plaintiff therefore wholly failed, and the only order that he would make would be to dismiss the action, with costs.

In the case of *Boaler v. Cochrane*, plaintiff sought a declaration that defendant vacated his office as director in 1897, as on that day he accepted a place of profit under the company. If he failed on that point, he sought a declaration that Cochrane ought to have retired in 1901, and that, as he was not re-elected on that date, he was no longer a director, and also that he could not vote in regard to certain shares, as there was money due and payable on them. The plaintiff's action in this case also wholly failed, and must be dismissed, with costs. In the case of *Oldfield v. Cochrane* and *Cochrane v. Oldfield* the questions raised were questions of internal management, and could be dealt with by the company in general. Both these actions would stand over a sufficient interval to allow a meeting of shareholders to be held. The motion *in re* the Companies Acts, he understood, was to be treated as abandoned.

Mr. Boaler now asked his Lordship to impound all the documents in the case. There would be a prosecution, and, that being so, he asked his Lordship to impound the documents.

His Lordship said he saw no reason whatever to impound the documents. They were produced quite readily, and he thought the proper course would be to give them back to the parties who produced them.

(*Acct. L.R.*, 1903, p. 23.)

The case of *Re THE COMPANIES ACTS, 1862 to 1880, AND
Re AUSTER, LIM.*

(Decided before Mr. Justice WALTON, in the Chancery Division,
on September 9 1903.)

*A Company struck off the Register for neglect to file the necessary Returns
may be restored, upon terms.*

This was a petition of Auster, Lim., whose registered office is the Crown Works, Barford Street, Birmingham, and of Alfred Auster and Arthur Collins Auster, coach and axle manufacturers, members of the company, that it might be ordered that the name of the company be restored to the Register of Joint Stock Companies in England, and that the company and all persons be placed in the same position as if the name of the company had never been struck off the register, and that the Registrar of Joint Stock Companies might be directed to advertise in his official name in the *London Gazette* the order of the Court to be made on this petition. In support of the petition it was said that the company was incorporated in 1897, and had continuously carried

on its business. On or about the 16th of November 1902 the Registrar of Joint Stock Companies in England, pursuant to Section 7 of the Companies Act, 1880, struck the name of the company off the register of companies kept by him, in accordance with the Companies Act, 1862, and notice thereof was published by him in the *London Gazette* on the 18th of November 1902. It was alleged by the Registrar of Joint Stock Companies that before striking off the company's name he duly sent the notices and otherwise complied with the provisions contained in clauses 1, 2, and 3 of Section 7 of the Act; but, through the negligence of one of the company's clerks, the notices were not communicated to the directors, secretary, or members of the company, nor did they come to the knowledge of the company's directors until July last. The petition was presented under the Companies Act, 1880, Section 7, Sub-section 5.

JUDGMENT.

Walton, J., made an order in the terms of the prayer of the petition, the petitioners undertaking to send in to the Registrar the returns now in arrear and to pay the costs of the petition.

(*Acct. L.R.*, 1903, p. 127.)

The case of REX v. WHITAKER WRIGHT.

(Decided before Mr. Justice BIGHAM and a Special Jury, in the King's Bench Division, on January 11 1904.)

*Prosecution of a Company Director under the Larceny Act, 1861, ss. 83 and 84.
Falsification of Accounts.*

The main facts of this lengthy case will be gathered from the Judge's summing up, which is reproduced below.

His Lordship, after congratulating the jury on the ending of the case, and counsel on both sides for the careful way they had dealt with the masses of evidence, said the charge against the defendant was in substance one of having issued in connection with the Globe Company two false and fraudulent Balance Sheets. The charge, however, was divided into no fewer than twenty-six different heads, and before they could find the defendant guilty they must be satisfied that the prosecution had brought home to him one or more or all those separate charges. To these counts it would be his duty to call their special attention, because he was going to ask them to find a general verdict of "guilty" or "not guilty." If they found a verdict of guilty, they would tell him whether in their opinion the evidence was not sufficient to support the

charge of any particular count. It was a serious charge—a very serious charge—against the defendant, and they ought not to find him guilty unless they were satisfied beyond all reasonable doubt of his guilt. There was one thing more. It had been said by Mr. Walton that a verdict of guilty against the defendant would involve in some sense a similar verdict against two eminent gentlemen—Lord Loch and Lord Dufferin—who were dead and gone. It would not do anything of the kind. They had not heard what these gentlemen had to say, or what could be said on their behalf. Their conduct, so far as they knew this case, was consistent with their having honestly made mistakes or with their having been simply negligent in matters with which possibly they were not so conversant as was Mr. Whitaker Wright. Let them not be deterred from finding the verdict which they thought they ought to find simply because it was suggested that by so doing they might cast a slur upon people who were dead. They had to decide the question of Mr. Whitaker Wright's guilt or innocence only with reference to the evidence before them. There was another observation. It was said as a reproach, he understood, that the prosecution had not called in support of their case some witnesses—particularly Mr. Lehmann, Mr. Macleay, and General Calthorpe—all of whom were alive. The least thought would show them at once that this complaint was one which was not borne out. Had they been able to throw any light on the case favourable to the defendant, Mr. Whitaker Wright was the person to have called them, and not the prosecution. They were available, they could have been called, and Mr. Whitaker Wright had not thought fit to call them. It was said again that the charge was a stale charge. Mr. Walton reproached our legal system, which included no provision similar to that under the civil law, that after a certain period a man could not be vexed by actions. Our criminal law allowed, and in his opinion properly so, no lapse of time to shield a man from the consequences of his crime. It would be a lamentable thing if it were otherwise. It was the object and interest of a criminal always to conceal his crime, and if he could successfully conceal it for a few years, as many could, he could then say that the time had gone by when he could be prosecuted, and he would escape. However long a man's crimes might be hidden from view, when they came to light, according to our criminal law, as he thought properly, the man was responsible to that law. He had disposed of these few topics, which were topics of prejudice that probably might influence their mind, and he begged the jury to discard them, and address themselves entirely to the evidence, so far as it touched Mr. Whitaker Wright, with the object of seeing whether the charges were successfully and clearly brought home. The offences with which Mr. Whitaker Wright was charged were contained

in the 84th and 83rd Sections of the Larceny Act of 1861. He put the sections in inverse order, because the first eighteen counts of the indictment were under Section 84, which made it a misdemeanour on the part of a director, manager, or officer of a public company to circulate or publish, or concur in making or circulating or publishing, any false statement of account with intent to deceive and defraud. Section 83 referred to falsifying the books and making entries in them, knowing them to be false. Of the eighteen counts under Section 84 nine related to the events of 1899, and nine to the events of 1900. Of the nine relating to 1899, four referred to the Balance Sheet and report of that year. The question they had to consider with reference to the 1899 Balance Sheet was whether it was false in the particulars mentioned in the counts of the indictment; were those particulars material; did the defendant know them to be false; and did he publish the document with intent to deceive and defraud.

The Judge, referring to the formation by the London and Globe of the British America Corporation and the Standard Exploration Company, pointed out that in little less than twelve months £400,000 on paper had become £5,000,000 on paper. This struck him as a most singular state of things.

Mr. Walton explained that the Standard and British America were new properties.

Mr. Justice Bigham said he was now told that these were new properties, but the jury had not previously heard that they were new properties, nor had they heard of any value put upon these properties which would stand at the back of this enormous increase of capital. But there it was. The jury must exercise their wisdom and discretion, and ask themselves what sort of a business was this which developed in this way? It was said that the cash position of the London and Globe, as shown in the Balance Sheet of 1899, was due to "the aim of the directors, extending over twelve months, to strengthen and maintain the position of the company during the past year." It was said by the prosecution that the statement as to the cash balance was untrue—that the transactions had not extended over the whole year, but that this vast sum of money had been brought together as the result of transactions hurriedly gathered together in two days, and had really nothing to do with "the aim of the directors, extending over twelve months, to strengthen and maintain the position of the company during the past year." The jury must use their common sense in dealing with this matter. Was it the result of hurried schemes and transactions rushed in at the last moment before the Balance Sheet came into existence, and entered into for the mere purpose of enabling them to make a statement

such as that laid before the shareholders? That was the representation relied upon in regard to this particular Balance Sheet. The jury must ask themselves whether the statement was really true, or whether it was a lie covered with the garb of truth. It would be necessary to draw the jury's attention to the way in which the money was got together. On September 29th the London and Globe had at its bankers about £80,000. It called in a loan of £84,000, which was quite legitimate, and also got £170,000 by a legitimate transaction in Nickel shares. They did not want to borrow, because the debt incurred would have to go into the liabilities. The money was raised by sales of property, for which a liquid asset, or cash, was gained. On September 29th Mr. Wright, managing director of the Standard Company, signed a cheque in favour of the London and Globe for £173,000, and that was paid into the bank, and formed part of the £534,000 in the Balance Sheet. The Globe sold 11,000 Lake View shares on the market, while the Standard Company bought 4,328. Then the Globe came to the conclusion to make the Standard Company their buyers, instead of the outside market. The Standard Company did not get all the shares, but they got a good many. All the Globe apparently had at that time was 3,048. Mr. Wright, however, came to the rescue by lending 2,938 of his own shares. With that assistance the number was made up, and the Standard Company gave a cheque for £158,000. That transaction was undone in a few days when the Balance Sheet was made up. Was it honestly a business transaction? Could it be justified by any code of "window-dressing" or any other code? The jury must decide whether all that was done for the mere purpose of swelling the cash balance in the Balance Sheet and so deceive the shareholders. That was what took place in September and was discussed at the meeting in October. Within a month they were told that that great flourishing institution, paying 10 per cent. upon two millions of capital, showing £500,000 placed to the Suspense Account, and a profit something like a quarter of a million in twelve months, was in such a state that if Mr. Wright had not come to its help by lending it £300,000 it would have come to the ground. In February 1900 it came out that the Globe had lost three-quarters of a million of money, and its allied company, the Standard, had lost another quarter of a million. Those gambling concerns, for they were nothing else, had squandered those sums—lost them, if they liked. Perhaps the indignation he felt when he thought of those transactions induced him to use language that was too strong. The Globe was in that state at the end of the financial year, September 30th 1900. Another gamble was started—another ring was formed by the creation of a syndicate. Had the unfortunate shareholders any notion of this ring? It was carefully concealed from them, and Mr.

Wright said it was perfectly right to conceal the fact, not only from the public, but from the shareholders. How it could be said, with reason, that when September 30th came, and the company was insolvent, it was the duty of Mr. Wright, or of anybody, to go on, and, in vain, attempt to retrieve the position of the company by speculating in Lake View shares, and to delay the publication of the Balance Sheet until that transaction had been made, he could not conceive. He entirely disagreed with the suggestion that it was his duty to the shareholders to delay the publication of that Balance Sheet. What was the extraordinary result of the transactions between September 30th and December 5th—two months? If the jury looked at the Balance Sheet, they would find that the company, which Mr. Wright himself said was insolvent on September 30th, had to the credit of its Profit and Loss Account £463,670. Let the jury observe the extraordinary state of things—a company admitted to be insolvent on September 30th, two months afterwards was not only solvent, but had a surplus of £463,000! Was it credible? And that Balance Sheet was produced at the meeting of December 17th, and put forward then as representing the position of the company. In ten days the company was hopelessly bankrupt, and it had since failed to pay its creditors. Those were the salient facts relating to the 1900 Balance Sheet. Let the jury consider how the position had been changed in two months, October and November 1900—how had it changed so that the company which was insolvent on September 30th had on December 5th nearly £500,000 to its credit? It arose out of a number of transactions, the like of which he, in a long experience, had never heard. On November 23rd 1900 the Globe had agreed to form a company called the Loddon Valley Gold Estates. The Globe guaranteed to find £50,000 of the capital of the new company, and in return got from the Victoria Company a property which had been referred to as the Option Block. It was not said what the property was really worth, but they were told that it had been sold for £10,000. On December 4th the Globe found a purchaser for £100,000—the Standard Exploration Company. They knew nothing of any report being before the Standard Company to show that the property was worth 100,000 pence. This Option Block came to the Globe when it was, so to speak, *in extremis*, and the £100,000 went into its Balance Sheet. Was that honest? Could it be justified? The common sense of the jury would decide. What was the next item? On November 6th the British America Corporation had formed a company called the Columbia Proprietary, with a capital of £350,000, and had received from the Columbia Proprietary £300,000 of its shares. These shares, like the "Option Block," were taken at once, and put into the Balance Sheet of the Globe. So far as they knew, there was nothing

to show that the shares were worth any substantial sum. It was on December 4th—the day before the Balance Sheet was issued—that the £150,000 shares were allotted to the Globe. Next there was the company called the Victoria Gold Estates Company, from which the Option Block came. In November 1899 the property of the Victoria was divided into halves, and two companies were formed, each with a capital of £750,000 or £1,500,000 in all. A property still in a state of development suddenly became represented by shares of the face value of £1,500,000. What then? By a series of operations the Globe got hold of the Standard's £35,000 of shares, and of the British America shares at par, and so got into its hands £200,000 of shares, becoming entitled to the whole of the four-sevenths. It then carried all these shares into its Profit and Loss Account at their par value, and so created a profit of £560,000 odd. There was a good deal of delay, which did not astonish him, Mr. Justice Bigham went on, in getting all the facts. The Attorney-General had declined to authorise a prosecution at the public expense; but he took his line of action on facts less complete than those which had been brought before the Court. Furthermore, the Attorney-General's view was that the shareholders who complained were the people who should prosecute, and not the public generally. What happened when the matter was before the Attorney-General the jury ought to dismiss from their minds altogether. After going to America, when the prosecution had been authorised, Mr. Whitaker Wright resisted extradition proceedings in America, though as soon as he landed he telegraphed to the Official Receiver expressing his willingness to return at once if he could be permitted to do so as a free man. On the whole, the Judge suggested, the jury might strike out the whole of the controversy as to whether Mr. Whitaker Wright did or did not "run away."

VERDICT.

The jury found the defendant guilty on all counts.

Mr. Walton then addressed the Court in mitigation of punishment, pointing out that previously to the present charges no imputation of any sort had ever been made against the defendant's integrity of character.

The Judge, in passing sentence, said:—In my opinion, the jury could arrive at no other conclusion than that which they have expressed in their verdict. I confess that I see nothing that in any way excuses the crime of which you have been found guilty, and I cannot conceive of a worse case than yours under these sections of the Act of Parliament. In these circumstances, I do not think I have any option except to visit you with the severest punishment which the Act permits, and that is that you go to penal servitude for seven years.

(*Acct. L.R.*, 1904, p. 13.)

The case of TOWERS v. AFRICAN TUG CO., LIM.

(Decided before VAUGHAN WILLIAMS, STIRLING, and COZENS-HARDY,

L.JJ., in the Court of Appeal on March 1 1904.)

Held that Shareholders who have received Dividends improperly paid out of Capital cannot maintain an Action against the Directors who caused such Dividends to be paid.

This was an appeal by the defendants against the decision of Mr. Justice Byrne, which was delivered on the 6th November 1903. The plaintiffs in this action were Mr. W. H. Towers, formerly secretary of the company, and Mr. P. Wedlake, a director of the company, and the plaintiffs sued on behalf of themselves and all other the shareholders of the company, except such of them as were defendants, joining as defendants the company, and the other two directors, named Alexander and Wood, and claiming payment by the defendant directors to the company (1) of £375 which it was alleged that the defendants ought to have recovered against an ex-director, instead of compromising with him; (2) £127 10s. alleged to have been wrongly paid as a dividend out of capital. All the other shareholders afterwards obtained an order joining them as defendants, and alleging that they acquiesced in both the compromise and the dividend. There was a counterclaim against the plaintiffs, in case they succeeded on the dividend point, to recover from them the shares of the dividend received by them, and they did not dispute their liability to refund these amounts. At an early stage of the hearing the learned Judge held that the first claim could not be sustained. The facts relating to the payment of dividend out of capital were thus stated by the learned Judge. The company was incorporated in 1896, and the plaintiffs' claim was for payment into the company's coffers by the defendants Alexander and Wood, as the company's directors and its trustees, of the sum of £127 10s., the amount of an interim dividend paid to the shareholders but never earned. The company had carried on business from 1896, and there were three directors, the defendants Alexander and Wood and the plaintiff Wedlake. Two directors were a quorum, and the plaintiff Towers was secretary to the company. In March 1900 the circumstances were as follows:—On the Balance Sheet for 1899, made up to July 31 1899 (the end of the company's financial year), there was a debit balance of £756 10s. 11d. In certain correspondence in March 1900, between Alexander and Towers, the secretary, Towers recognised that from August 1 to December 31 1899 the company had made a profit of £300, but contended that until the debit balance was wiped out payment of the interim dividend then proposed would be paying it out of

capital, and that this would be illegal. Alexander and Wood took the other view, and the dividend was shortly afterwards paid on the faith of a resolution signed by them, Wedlake taking no part in this. On the assets side of the Balance Sheet, up to July 31 1900, there was an item of "Dividends not earned, £127 10s.," and to make this side of the account balance with the other side (liabilities) there was an item, "Profit and Loss Account, as at July 31 1899, £756 10s. 11d., less profit for year, £245 18s. 4d. = £510 12s. 7d." The Balance Sheet, with these entries, was approved by a meeting of the directors, and also by a meeting of shareholders in September 1900. The meetings had also before them a report of the Auditor, explaining the insertion of these items, and stating that the interim dividend was unearned, and it was illegal to pay dividends unless they were earned, and that directors were liable in such a case, as it amounted to paying dividends out of capital. The entries in the Balance Sheet were in accordance with the mode in which the company's accounts had hitherto been kept. Mr. Justice Byrne held that the defendant directors must replace the £127 10s., with interest at 4 per cent. His Lordship said that the plaintiffs had allowed a considerable time to elapse before complaining of these matters, but they now asked that the defendant directors might be ordered to pay the company the amount of the interim dividend. The act complained of was *ultra vires* and the directors concerned in it were liable to the company in respect of it, and the fact that one of the plaintiffs was party to what was done did not stand in the way; and this seemed to be the case, although shareholders who received their shares of the dividend knew of the illegality. Towers, of course, would have to repay the dividend received by him. Article 36 authorised dividends to be paid to "the members according to their rights and interests in the profits," and Article 37 empowered the directors from time to time to "pay to the members such interim dividends as in their judgment the position of the company justifies." There was no question as to the dividend having been paid honestly or *bonâ fide*, but his Lordship said he must accept Mr. Norton's argument on this point. The directors knew from the books that there was no profit available for the interim dividend. They knew that for some months profits had been made, but that did not justify the payment. The plaintiffs came here insisting on the legal rights of the company to have the amount replaced. His Lordship could not say that Wedlake, suing on behalf of the shareholders, was not entitled to complain, and there must be an order on the defendant directors to replace the £127 10s., with interest at 4 per cent. But his Lordship understood that the company had lately had a windfall which at the end of the year would enable the whole of the deficit to be made up, and he thought that the accounts might be put in a form which

would render it unnecessary to have the £127 10s. actually repaid. The order must not, therefore, be acted on until after the next general meeting. The defendants were entitled to judgment on their counter-claim for the portions of dividend received by the plaintiffs, but this order would be stayed in like manner. The defendant directors appealed.

JUDGMENT.

Their Lordships allowed the appeal.

Lord Justice Vaughan Williams upon the whole did not think that the plaintiffs were entitled to relief. It was perfectly clear that they were aware of all the facts when they took the dividend. What, then, ought to be done with this action? There was no doubt that the payment of this interim dividend was *ultra vires*. One must start with the assumption that, if an act was done by a company which was *ultra vires*, no acquiescence in or ratification of that act by the shareholders could convert that which was *ultra vires* into that which was *intra vires*; it must be *ultra vires*. Now, if it was the fact that the plaintiffs knew of all that had been done, and had received dividends with full knowledge of all the circumstances, and then brought this action, ought they to be allowed to maintain the action? His Lordship thought not. He thought that an action could not be brought by an individual shareholder complaining of a matter which was *ultra vires* if he himself had in his pocket at the time he brought the action the proceeds of the act which was *ultra vires*; and in the same way it did not alter matters if he was suing for himself and other shareholders. Now, this dividend was in the pockets of the plaintiffs when the action came to be brought, and his Lordship felt bound to say that in this particular case there was a strong inclination in his mind not to give the plaintiffs the relief they asked. The fact of the payment of the dividend out of capital appeared on the face of the Balance Sheet, and the directors were minded to replace that capital, and had every prospect of doing so, even out of that very year's profits. This action was wholly unnecessary and wholly uncalled for; and his Lordship was of opinion, under the circumstances, that the Court was not bound, when it saw that the act *ultra vires* was in course of being put right, and would be put right, to accede to the plaintiffs' contention. This appeal should, therefore, succeed.

Lord Justice Stirling also thought that the appeal should succeed. This was a case in which no one suggested that there had been any fraud or dishonesty on the part of the directors or anyone else. The directors had, in paying the dividend out of capital, made a mistake, and no one charged anything against them but mistake. The facts

were perfectly open upon the Balance Sheet, and of course they there appeared. And further, the subsequent dealings seemed to show that the company did not intend to overlook the fact that this dividend had been improperly paid, and that there was no intention on the part of anyone but to do what was right and to pay back to the company what had been improperly paid. Such, in his Lordship's opinion, was the result of the Balance Sheet. Moreover, it appeared that the plaintiffs themselves had acquiesced from September 14 1900, when the company knew the facts, down to March 1903, when this action was brought. His Lordship thought that the proper inference was that the company was to go on and wipe out year by year parts of the deficiency, and that they intended when this improper dividend had been replaced to go on paying a proper dividend. There was no ground on which the Court ought to compel payment of this small sum; and, in truth, Mr. Justice Byrne, although he gave judgment in favour of the plaintiffs, so far from directing immediate payment, ordered that it should not be enforced, in order to see the result of future trading, and whether the sum would not be wiped out. That, it seemed, would have been done even if the action had been dismissed.

Lord Justice Cozens-Hardy was of the same opinion. It was clear that a payment by the directors of a company of a dividend out of capital could not be ratified by the shareholders. An action arising out of an act *ultra vires* ought properly to be brought by the company; but it had long been well established that there were cases in which such an action could be maintained by a shareholder on behalf of himself and other shareholders against the company as defendant. His Lordship would not pause to consider under what circumstances such an action could be maintained, but he thought that the present was such an action as could be maintained in point of form. But an action of this kind must be brought by a person who was really interested; and it had been clearly proved here, and indeed admitted, that the plaintiffs took this dividend with full notice of all the facts. It was also clear that this dividend, which they took with full notice that it had been paid out of capital, they had in their pockets at the time the action was commenced. Now, could a shareholder who had the money in his pocket maintain an action against the directors for repayment of the dividend on the ground that it had been paid *ultra vires*? His Lordship thought he could not. It might be that there was no direct authority upon the point, but the *dictum* of Lord Justice Brett in *Flitcroft's* case (21 Ch.D. 519) was, though only a *dictum*, very nearly in point. The Lord Justice said this (p. 534):—"I think that there was no ratification at all, because the assent of the shareholders was procured by improper accounts, the untruthfulness of which the share-

holders did not know. But suppose they had known it, I think that what was done was a breach of trust which they could not ratify. If they had with full knowledge assumed to ratify what was done, they could not individually have complained, but the shareholders are not the corporation." Lord Justice Brett assumed that a shareholder who had ratified could not individually have complained; and it was equally true that a shareholder who had the money in his pocket could not have any greater right merely because his action was by himself and on behalf of all other shareholders. In fact, he must succeed if at all by his own merits and not by the merits of others. His Lordship thought that the judgment of Mr. Justice Byrne in the action must be set aside, and that there should be judgment for the defendants upon their counterclaim, with costs.

(20 *Times Law Reports*, 292.)

The case of SHORT & COMPTON v. BRACKETT.

(Decided before His Honour Judge TINDAL ATKINSON, in the Colchester County Court, on 6th May 1904.)

Held that an Accountant making an Investigation of Accounts for an Incoming Partner is entitled to assume that the books are correct.

Messrs. Short & Compton, Chartered Accountants, of Colchester, sued Mr. Brackett, of the Hythe ironworks, to recover 30 guineas for services rendered in the preparation of certain accounts, and there was a counterclaim for £139 damages for alleged negligence on the part of the plaintiffs.

Mr. Jones said Mr. Brackett was proposing to take a partner, and employed the plaintiffs to prepare accounts from his books, which would show the amount of the profits and the goodwill. The return furnished by Messrs. Short & Compton showed that the profits during a period of three years and two months had been £929. Nine months afterwards Messrs. Short & Compton sent in their bill, when Mr. Brackett wrote stating that he had recently discovered that, during the period covered by their investigation, a certain clerk of his was deficient in his account to the extent of £111, and alleging that, owing to plaintiffs' failure to detect this he had lost in the same way another £128. He added that, under the circumstances, he declined to pay plaintiffs' account. Mr. Jones added that the clerk mentioned, "who appeared to have since been allowed to abscond," seemed each week to have made out the wages bill for a larger amount than was due to

the men, and had himself kept the balance. This, Mr. Jones urged, could not have occurred but for the slipshod way in which Mr. Brackett kept his accounts. Messrs. Short & Compton, replying to Mr. Brackett's letter, stated that they were in no sense responsible for the entries in the books—their responsibility began and ended in putting before Mr. Brackett the result of his trading.

Mr. Compton said he was not instructed to audit, but merely to make up the accounts required from the books.

Mr. W. M. Blake corroborated.

Mr. C W. Cornish, Fellow of the Institute of Chartered Accountants, said that in the case of preparation of a Balance Sheet from books the totals in the books would be assumed to be correct without investigation, and it would not be the duty of an accountant to examine vouchers, in which term he included Wages Books.

Mr. Macklin urged that one of the primary duties of an accountant was to ascertain that accounts were accurately kept. Mr. Brackett placed before plaintiffs all his books, and asked them to make a thorough investigation.

With regard to the disappearance of the clerk alluded to, defendant said he sent him off on the day he discovered the deficiency.

Called for the defendant, Mr. Ernest H. Frith, a member of the Institute of Chartered Accountants, of London, said he considered that it was the duty of an accountant, when making up accounts in connection with the admission of a new partner, to investigate vouchers and the Wages Book. He agreed that the Wages Book was of the nature of a voucher and in the present case could not be treated as a book of account.

Cross-examined: The fact that the principal of the business himself drew the wages cheques would make no difference to his desire to see the Wages Book.

JUDGMENT.

His Honour Judge Tindal Atkinson held that, having regard to the object for which they were employed, the plaintiffs were entitled to assume that the figures appearing in the defendant's books as paid for wages were correct, and in view of the fact that at the time there was no suspicion of any falsifications by the defendant's clerk alluded to, he thought there was no negligence on their part. Therefore judgment would be for plaintiffs on the claim with costs, and the counter-claim would be dismissed with costs.

(*Acct. L.R.*, 1904, p. 85.)

The case of the LONDON OIL STORAGE COMPANY, LIM.
v. SEEAR, HASLUCK & CO.

(Decided before ALVERSTONE, C.J., and a Special Jury, in the King's
Bench Division, on 1st June 1904.)

*Held that it is the duty of the Auditor of a Company to take proper steps to verify
the existence of Assets stated in the Balance Sheet.*

This was an action for damages for alleged negligence in auditing the plaintiff company's accounts. The defendant firm denied that they had been guilty of negligence, and said that the alleged loss of £760 had been caused by negligence on the part of the directors of the plaintiff company in entrusting so much money to their cashier.

Mr. Banks stated that the defendant firm consisted of a Mr. Hasluck, who for many years had been the Auditor of the plaintiff company, which was incorporated in 1885 to take over a business, till then carried on by Ingall, Phillips & Co., consisting in the storage and lighterage of oil. The plaintiff company had three wharves on the river Thames—Palmer's, Melhuish's, and Dudgeon's. The defendant had been the Auditor of the company from the first, and it was his duty under the articles to audit the accounts and "to certify the correctness of the financial statement" for the purpose of the yearly Balance Sheet, in which there appeared a sum representing cash in hand, and it was in reference to that sum that the plaintiffs alleged that Mr. Hasluck, through his clerks, had been guilty of negligence. One of the officials of the company had been a Mr. Frederick R. Clarke, who had been taken over from Messrs. Ingall when the company was formed, and who had at first been bookkeeper and cashier, but was later also appointed secretary at the City office. At that office a Petty Cash Book was kept, in which the cash balance appeared, and Mr. Hasluck's clerks entered in the Balance Sheet the amount of petty cash that appeared in the Petty Cash Book, but they never troubled to find out whether Mr. Clarke had that balance in hand or not. Till 1902 nothing was suspected, but Mr. Clarke was then seized with a paralytic stroke and had ever since been in a pitiable state and could not be called as a witness. His duties were taken over by Mr. Hubble, who found in the cash box about £30, though the Petty Cash Book showed a balance of £796, the balance having gradually increased from £21 in 1897 to £796 in 1902. Mr. Hasluck's attention was called to the matter and he said that some people never saw further than their noses. Counsel submitted that the circumstances were suspicious and ought to have put the Auditor on inquiry.

Mr. Thomas George Redgrove, the plaintiffs' manager, gave evidence in support of counsel's opening. In cross-examination he said that Mr. Clarke had always been a trusted servant of Messrs. Ingall.

Mr. Henry Thomas Hubble, who had been Mr. Clarke's assistant, and who succeeded him, stated that the Petty Cash Book was kept in a safe of which Mr. Clarke kept the key. When Mr. Clarke was there witness had no access to it. The only occasion when Mr. Clarke was absent for more than a day or two was in 1900.

Mr. George B. Gane, a director of the plaintiff company, said that he had had complete confidence in Mr. Clarke. Witness never asked him how much cash he had in hand, nor did he look at the entries in the Petty Cash Book.

Mr. Isaacs, for the defence, said that Mr. Hasluck had acted as Auditor at 35 guineas per annum, and this involved the attendance of his clerks at the office for six or eight weeks. In considering what his duties were, the amount of his remuneration ought to be taken into consideration. It was extraordinary that the directors never took the trouble to ask Mr. Clarke how much he had in hand. There was nothing to excite Mr. Hasluck's suspicions. The directors were not suspicious, and yet they said that Mr. Hasluck ought to have been. An Auditor was entitled to act upon the representation of a trusted servant of the company. The plaintiffs had not proved that the money was not taken after the last audit. If it was, the Auditor could not have found out the deficit.

Mr. Lawrence Hasluck said that he had no reason to doubt Mr. Clarke. Witness knew the confidence reposed in him by the directors. Witness having ascertained the creation of an asset by vouching items on both sides did not ascertain the actual existence of it. The amounts shown by the books to be in hand never excited his suspicion. Witness's remark about people not seeing further than their noses referred to the directors, and not to his own clerk.

Mr. Bankes: You audit the books of a good many companies?—Yes.
I suppose your fees vary?—Yes.

You get as much as you can?—No, I get as much as they will give me. (Laughter.)

You do not suggest that your duties depend on the amount of your remuneration?—No, but the Court of Appeal have suggested it.

Witness considered that his duties ended when he had seen that the entries in the books created an asset. But if there was any ground for suspicion he should report the matter to the directors.

The Lord Chief Justice, in summing up to the jury, said : Gentlemen of the jury, this is an important case, and the law on the matter you will be good enough to take from me. If I direct you wrongly I can be put right afterwards. It is your duty to take the law from me, but the facts will be entirely for you ; and if I, in the course of my address to you, indicate any opinion on the facts, do not think it is meant to dictate to you, but only to direct your attention to the points for your consideration as they occur to one having had some experience of accounts of this kind.

The case is of importance, in the first place, to the parties themselves, because the claim made against a professional gentleman is for a considerable sum, some hundreds of pounds, and it is important for the reason Mr. Bankes points out, that it raises an important question as to the duty of Auditors. The best thing I think I can do to make it clear is to direct you as best I can as to the law of this case, and then go through the facts bearing upon the question of law, so that we may be able, if we possibly can, to keep our heads clear in considering how the case has to be dealt with.

Now, there are two or three matters which I think you should dismiss from your minds altogether. You have not to consider for a moment whether Mr. Hasluck has been sufficiently remunerated or not. What Mr. Bankes said is perfectly right. He has accepted the position and duties of an Auditor, and you have not to consider, aye or no, if he has had a sufficient amount, you have also not to consider as a substantive matter whether or not the directors have been negligent. I entirely agree with the view of the law as explained to you by Mr. Bankes, that the Auditor cannot shelter himself for any breach of duty under the neglect of the directors ; he is there to do his duty to the company ; the only point on which the conduct of the directors may become material is upon the subordinate question as to whether there is anything to arouse the suspicion of the Auditor, and whether or not the loss has really been occasioned by the Auditor's conduct.

Now, dismissing those two points, except so far as I may have to refer to one later on, let me tell you the duty of the Auditor. The Auditor is an officer contemplated by law to protect the interests of the company and its shareholders as such ; he is there having certain duties prescribed by Act of Parliament, certain powers prescribed by Act of Parliament, and certain powers prescribed by the articles of association of this company. They may vary, but not very materially, in the case of different companies. We have simply to do with this company. The Auditor most undoubtedly does undertake very considerable responsibilities, and is liable for the proper discharge of his duties, and if by

the neglect of his duties, or by want of reasonable care, he neglects his duty, and damage is caused to the company as such, he is responsible for that damage. I will not adopt any fanciful expression which may be quoted from any particular judgment, but he has got to bring to bear upon those duties reasonable and watchful care, he has got to discharge those duties remembering that the company look to him to protect their interests. He is not, however, supposed to be a man constantly going about suspecting other people of doing wrong, and that is the only respect in which, I think, Mr. Bankes in his most able speech pressed the matter a little too high. While Mr. Hasluck has by the exercise of due and reasonable care to see that all the officials of the company are doing their duty properly in so far as the accounts are concerned, he is not bound to assume when he comes to do his duty that he is dealing with fraudulent and dishonest people; and there comes in the most important consideration from one point of view—perhaps more important than the other, though I do not think of such substantial weight in this matter—if circumstances of suspicion arise, it is the duty of the Auditor, in so far as those circumstances relate to the financial position of the company, to probe them to the bottom.

Now, I have stated, I hope clearly, the general position of the Auditor, and I do not think it necessary to elaborate it at very great length, beyond reminding you of certain specific articles, which in this particular case do prescribe the duty of the Auditor. I thought when Mr. Bankes opened the case, and I still think, he did not in any way overstate the duty that falls upon an Auditor in connection with such articles of association as these. Whether or not he has applied the rule correctly to the facts is a matter that you will have to consider later on. The articles provide:—"Once in every year—namely, preparatory to each ordinary general meeting—the accounts of the company shall be examined, and the correctness of the financial statement ascertained by one or more Auditor or Auditors." They further provide that "every Auditor shall be supplied with a copy of the financial statement intended to be laid before the next ordinary meeting, and it shall be his duty to examine the same with the accounts and vouchers relating thereto." And further: "He may, at the expense of the company, employ accountants or other persons to assist him in investigating such accounts, and he may in relation to such accounts examine the directors or any officer of the company." Although that is written down in writing in these articles of association, which I gather were dated somewhere about the year 1885, they really do not do much more than put in plain and simple language that which would be the duty of an Auditor almost derived from his position, but it is of importance to remember that in order to strengthen in one sense the hands of

Auditors, and at the same time to make it clear that their duties were not those of guarantors for the honesty of servants, were not an undertaking to the company that there had been no fraud or crime committed upon them. Section 23 of the Act of 1900 also specifies the duty of the Auditor in such plain language that I will venture to detain you for a moment by reading it to you:—"Every Auditor of a company shall have a right of access at all times to the books and accounts and vouchers of the company, and shall be entitled to require from the directors and officers of the company such information and explanation as may be necessary for the performance of the duties of the Auditors, and the Auditors shall sign a certificate at the foot of the Balance Sheet stating whether or not all their requirements as Auditors have been complied with, and shall make a report to the shareholders on the accounts examined by them, and on every Balance Sheet laid before the company in general meeting during their tenure of office; and in every such report shall state whether, in their opinion, the Balance Sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company." Now, you must not think that those words "as shown by the books of the company" excuse the Auditor from making proper inquiries into any particular entry in the books. The question always becomes, what, under the circumstances of the case, is a proper inquiry to make in every particular case; and that is why, although it is quite easy for me to lay down to you in general terms what the duty of an Auditor is, it is very much more difficult for you, or for anybody else—for me or for you either—to apply that duty to the particular case.

That is why I wish for a very few moments to consider with you the application of this duty to the facts of this particular case. In the same way, Mr. Isaacs is quite right in saying to you, as I have already indicated, that the Auditor is not bound to assume that people are dishonest. On the contrary, he is entitled to think that they are honest, and I only read to you for the purpose of an observation I wish to make the passage in which that is put in the Court of Appeal:—"He is justified in believing tried servants of the company in whom confidence is placed by the company. He is entitled to assume that they are honest, and to rely upon their representations, provided he takes reasonable care. If there is anything calculated to excite suspicion he should probe it to the bottom, but in the absence of anything of that kind he is only bound to be reasonably cautious and careful."

Now, I think the best concluding direction I can give to you for which I am responsible is, that he must exercise such reasonable care as

would satisfy a man that the accounts are genuine, assuming that there is nothing to arouse his suspicion of honesty, and if he does that he fulfils his duty; if his suspicion is aroused, his duty is to "probe the thing to the bottom," and tell the directors of it, and get what information he can. And apart from the circumstances of this case, I think Mr. Hasluck made an answer which shows that he appreciated his duty when he said, "Had I any reason to think that the amount of cash retained at the city office was too much, I should have gone to the directors and asked for an explanation; that would have been my duty," and so far as I may express an opinion, I think that is a true view of what his duty would have been under the statute and the articles. He ought, if his suspicion was aroused by anything that was called to his attention, to have gone to the directors and asked for an explanation.

Now, gentlemen, I am bound to say that I feel that the plaintiff has a perfect right to press upon you that the defendant's clerk (who, I think, was called Percy Clark) was not called before you, because I am bound to tell you that the defendant is responsible for want of reasonable care by his clerks. This is a part of the work which cannot be done by the defendant only himself. Some of the work must be done by his clerk. He has said and gave his evidence most fairly, I think, whatever the consequence may be, "looking back at it I can see nothing to blame my clerk for." But you have to consider if either the defendant or his clerks through whom he was doing the work have failed to discharge their duty properly, or have been guilty of want of reasonable care; you must not press it too hard. I do not think Mr. Bankes used it at all unfairly, or pressed you too much upon it; for myself, it would have been more satisfactory if one had had some explanation as to what came to the knowledge of the clerk as to the cash in hand at the time. It is entirely for you, when you have considered what are the facts of this particular case, to exercise your own judgment as to that and take it into consideration, because if you come to the conclusion that, *primâ facie* not sufficient inquiry having been made, the defendant has not put all the information he might before you, you are entitled to draw inferences from that from the absence of the clerk. Beyond that you ought not to go.

Now, gentlemen, Mr. Bankes, on the part of the plaintiffs, shapes his case in two ways. The first of them is that it is the duty of an Auditor to check an asset such as is called and known as "cash in hand." Secondly, he says it is admitted that if circumstances of suspicion arise, the Auditor ought to "probe the thing to the bottom," and he says "I (Mr. Bankes) suggest to you on behalf of the plaintiffs that there were grave circumstances of suspicion in this case." It is entirely for

you and not for me, but it seems to me in this case the first branch of Mr. Bankes' argument is the most important. Aye or no, were proper or sufficient steps taken to verify the cash in this instance? And, subject to your better judgment when I come to discuss the evidence as to the second branch of the case, I should have thought, if it was necessary to rely upon what Mr. Bankes called circumstances of suspicion, you would have much greater difficulty in dealing with the case. I now, for the purpose of the first question, will consider the evidence as to what may be called the *primâ facie* duty of an Auditor to verify an important asset, and I shall ask you presently as business men to be good enough, as this is a very important case, to take the documents, and not simply accept my comments—to take the books—and you can find your way quite easily through them as business men. Now, I should have thought that is why this is the important proposition—That it could be scarcely disputed that it was the duty of an Auditor to verify the cash in hand. How it ought to be done in a particular case is more difficult, but *primâ facie* when a Balance Sheet is presented to an Auditor it does not matter if the Trial Balance Sheet should come to him or not, but I will take the Trial Balance Sheet which undoubtedly did come to him. When the Trial Balance Sheet of 1898 came to him, and he found among the items an item of £135 cash, and he found that it did mean cash somewhere that should have been vouched in some sort of way. Please understand, when you come to consider this case, if you think that is putting it too high it is for you, and not for me; I only tell you how it strikes me as to the evidence. I think that may be made plain by taking the case of auditing the accounts of a large shop with several branches. Suppose in the interests of the shareholders it was necessary to know the cash in the till. Suppose there was a large establishment with branches at half-a-dozen places, the Auditor auditing on various days, and there was said to be £500 in the various tills, made up of £50 in one place and £100 in another, and so on. I do not think anybody would dispute he ought to ascertain that the cash was there, and that is a way of stating the proposition which makes it plain on one side. On the other hand, when dealing with a business where money is being used by a particular branch, and one branch owes another so much money, it might be that the report upon a certificate of a qualified manager or secretary, or voucher of some sort of that kind, would be amply sufficient justification to the Auditor for passing the item.

The real difficulty in this case, as I think you will see on looking at the accounts, and upon which I do not wish to express the slightest opinion, is, aye or no, has Mr. Hasluck satisfied you in that respect he

has discharged his duty? I put it rather upon him, because I think it ought to be taken, and he does not really dispute it, that he has got to vouch and be satisfied with the correctness of the items in the Balance Sheet. That being so, has he done it sufficiently? Now, here comes the difficulty. It has been suggested as though the preparation of these things depended in the first instance on Mr. Hasluck. That is why I think Mr. Bankes may have pressed too much the question of the mere amount of cash supposed to be out. Now, the first that he gets is a Trial Balance Sheet of 1898, and that contains the five items at which you ought to look: the cash at Melhuish's, that is one of the wharves—I have marked them, gentlemen, in blue, so that you will see them in each year—£14 one wharf, £8 another wharf, £15 another wharf, and £133 the city office. Now, it is very difficult to express any view upon this without apparently indicating more to a jury than one ought, but take the question of the small item of cash supposed to be at the three separate wharves—£14, £8, and £15. In order to test that being there the man ought to have gone to the wharves and seen the money, or had it brought to him, or, it may be, some voucher given to him. Mr. Bankes does not complain in this action directly of those three amounts which form part of the total sum in hand, which in that year was £171 10s.; he does not complain of those three items not being examined; what he does complain of is that there is no evidence before you of £133, which is the balance, ascertained by taking the petty cash and subtracting the credit side from the debit side, that the city office owed to the business. I shall ask you to look at that account, and to see whether you come to the conclusion that under all the circumstances of this case it did show a want of reasonable care on the part of Mr. Hasluck and his clerk not to have investigated whether that £133 was really there. I postpone speaking of that particular year, and saying that it ought to have attracted suspicion, because it had gone from £21 to £133, as that relates to the part of the case dealing with the question of there being circumstances of suspicion. Then you come to 1899. In the same way you will find there are four items there, the total amount being altogether somewhere about £500, or very nearly £500. I think £479 of that is due to the city office—that is to say, it is item 748. If you turn back to the item 748 you will find there the city office received so many hundreds or thousands of pounds, and £479 was due to the office. You have to ask yourselves, under the circumstances of this particular case, was the Auditor whose duty it is to be satisfied that that is a true asset entitled to do no more than this gentleman admits that he did—namely, verify that the secretary had acknowledged the receipt from the company of, we will say, £2,000 or £3,000, which represented the gross receipt in that twelve months' expenditure—£1,900, or whatever it was on the other

side? and admitting that the office owed the business that amount, if you think he did enough there would be no question of breach of duty as to that. If you think that, looking at this quite apart from the question of there being big and small items, a reasonably prudent accountant would not have let that item pass without saying the £479 was somewhere, and where it was, you will have to express your opinion whether there was a breach of duty on the part of the defendant in that respect or not. I need not take you through the other items. I have marked them in blue, and I ask you to look at them in the trial sheets, because you have to make up your minds and be satisfied that the defendant discharged his duty in ascertaining that the cash balance was somewhere available, upon such evidence before him that you—as reasonable men—think he did enough. I do not want to repeat it. I am sure you understand me. He had before him original and genuine entries not challenged, showing the office had received in one twelve months £2,600, that they had spent a sum of £2,000, and that the head office therefore owed the business £600. He does not allege that he asked for more than seeing and checking that those were truthful business entries. If you think that in such a business so conducted it was his duty to ascertain that the cash was there, quite apart from circumstances of suspicion, of course you will not hesitate to say so.

Now, gentlemen, that is the part of the case so far as it depends upon the *prima facie* duty of the Auditor to verify the asset. It cannot be disputed that when an Auditor returns to the shareholders an entry of cash in hand he must have taken reasonable steps to ascertain that the cash was in hand. That does not enable you to answer the question without considering what he has done, because there may be cases in which he would be justified in acting on the representation of a cashier, or a servant whom he had no reason to distrust; and, on the other hand, there may be cases when he ought to go further and examine. You will have to say, when you come to consider the matter, within which of those categories this case falls.

Now I come to the question of the circumstances of suspicion, and, though I express an opinion with the greatest diffidence, it seems to me that the case for the plaintiffs is not so strong as it may be put with reference to the non-verifying. It is said "You, the Auditor, ought to have known that for a man to have these increasing balances due from the city office to the business was something suspicious." Now, on the mere question of amount, there was one fact mentioned that I think ought to be mentioned in the defendant's favour. Mr. Bankes says when it jumped in 1898 from £21 to £133 that ought to have aroused suspicion. It had been up to £136 three years before, and the mere

question of amount therefore would not seem to me to be of importance, but you have to consider for yourselves, is the fact it had got to £133, and the next year went to £479, to be considered or called by the Auditor and his clerks a suspicious circumstance? Now, gentlemen, here I do not think it is at all unfair to the plaintiffs to say it may be pressed too hardly against the Auditor. I think to this extent he is within the authorities and the ruling laid down by the Court of Appeal that he is not bound to criticise the policy of the directors, and if he finds for a series of years larger amounts have been left in the hands of the cashier than at first sight would seem to be required I do not think there is any *primâ facie* duty upon him to inquire into that. It is a matter of policy and not of audit. If it becomes suspicious, then you will understand that different considerations arise. But I confess, on the mere question of holding a larger amount, that that seems to me to have been pressed rather too far. Mr. Bankes called it, you know, "Petty Cash," but that is not quite the way I think you as city men will regard it. The items were arrived at by including the lighterage wages and the petty cash in the cheque. It is perfectly true that the smaller portion of this cheque was made up by the petty cash, but the lighterage charges went through this same head office account, and they did amount to as much as £50 or £60 a week, and it is not right to speak of it as a demand for petty cash only; but there is the fact, he had several hundred pounds more than was wanted for the larger expenditure he had to make, and I cannot do better than indicate to you what Mr. Bankes brought out in evidence to-day, which puts it very clearly in the six months up to the middle of October 1898, having had a balance of £133 on the 1st of May, he drew £1,585 and spent £1,300—that is to say, he would have increased his balance during the six months by about £300. Then in the next six months he drew £1,245, and spent £1,050, which would have increased it by £245. Gentlemen, it seems to me fair to say that, apart from any circumstances that aroused suspicion, the fact that the directors, who must be assumed to know something of the business from week to week, let this amount of money remain would be a circumstance of itself. An Auditor ought not to act blindly; but still, he ought to take it into his consideration. It seems to me difficult to say it was a circumstance of suspicion. If the retention of a large balance by the city office did not arouse the suspicion of the directors, it does seem rather hard to say that it ought to have aroused the suspicion of the Auditor. You will understand that I do not put this as taking away from his duty to examine the cash balance. I only deal with it as a circumstance of suspicion. There are five periods when the directors must have known of it, and that must not be lost sight of, that is when the Balance Sheet came out. I shall have to

refer to the lumping together of the cash in hand and bank balances, but there are four periods when it is the duty of the directors to apply their minds as to how the business is being conducted, and that is the £133 in 1898, the £574 in April 1899.

Mr. Bankes: That is when it is lumped, my Lord.

The Lord Chief Justice: I will refer to it in a moment. £479 in April 1899, £624 in 1900, £625 in 1901, and £681 in 1902.

Mr. Bankes: Not in any account that came before the directors, my Lord.

The Lord Chief Justice: I assure you I have not forgotten it, and I am doing my utmost to state it fairly. I did not say which "came before the directors." I avoided that because I was coming to it. I said "in the accounts of the company." The account I have is the Trial Balance Sheet, and the books of the company. I dare say it did not come before the directors.

Now Mr. Bankes says it was a suspicious circumstance that in the year 1899 it was lumped with the banker's balance, and that ought to have aroused the suspicion of the Auditor. It is very easy to be wise after the event, but unless the fact that there was so much cash in hand, which undoubtedly did come to the knowledge of the Auditor, was in itself a suspicious thing (and that is entirely for you), why its appearing in one item can be thought to increase the suspicion I have a difficulty to understand. In the Trial Balance Sheet sent to the Auditor it is not lumped at all, but treated as a separate item. It is true, in the final Balance Sheet, and I dare say in the draft that went before the directors, it is lumped, but, as the directors told us the bank Pass Books were before them at every meeting, it is entirely for you—do not take my judgment. If you should be of opinion there was nothing suspicious in the fact that there was this comparatively large balance in the hands of the cashier, it will be for you to say if the fact that he lumped it in the final Balance Sheet—after having told the Auditor the details of it—was, of itself, a circumstance to arouse the Auditor's suspicion. Mr. Bankes presses you to say the directors may have known nothing except what appeared in the rough Balance Sheet which came before them, or the final Balance Sheet which the Auditor signed. Whatever be the fact as to that, it is entirely for you. The substantial matter would seem to me to be, aye or no, whether this circumstance of the large balance was enough to arouse the suspicions of the Auditor.

Now, gentlemen, I come to the other part of the case, on which the absence of the clerk does present a very great difficulty. You may be of opinion that some inquiry should have been made with regard to

where this cash was : that the mere fact that when you are dealing with a company of which the profit and loss or the turnover is about £21,000 a year, and the total paid-up capital is only £47,000, that an item such as several hundred pounds "cash at bankers" is enough to require a proper examination. Of course, the real difficulty that you are in here is that we do not know what did pass between the clerk, Mr. Hasluck's representative, and Mr. Frederick Clarke, the fraudulent cashier. Of course, if Mr. Clark, Mr. Hasluck's representative, asked where that balance was, and was given a satisfactory explanation, either by the money being forthcoming or by a statement which an honest man may have believed, a very different consideration would arise; but for reasons which we do not know, and we are not entitled to speculate more, except that Mr. Bankes is entitled to say it was the duty of the defendant to put all he could before you, as to what explanation could be given to you by the clerk, and I am bound to tell you that if Mr. Frederick Clarke gave to Mr. Hasluck's representative an explanation which was not satisfactory, and which ought to have aroused Mr. Hasluck's clerk's suspicions, Mr. Hasluck is responsible. That is a part of the case which, unfortunately, is left in the dark. We do not know. Mr. Hasluck cannot say "I never saw that Cash Book myself, but I am sure I saw the entry of £133 and £479 and £624, because they are on these papers that I have ticked." But whether or not he was acting on a vouching by his clerk which was not satisfactory we do not know. It is entirely for you. I tell you it is the *prima facie* duty of Mr. Hasluck to satisfy you that he has properly fulfilled his duty of seeing that that asset was there, and it will be for you to say whether or not he has discharged his duty in that respect. The final certificate he gave is this. He first, in accordance with the Act, certifies that all their requirements as Auditors have been complied with. Whatever that is, he made inquiries of the directors and they concealed nothing from him. "We have audited the above Balance Sheet, and in our opinion such Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company." That does not mean in any way to discharge Mr. Hasluck of the responsibility of ascertaining whether an asset put down did in fact exist, and, as Mr. Bankes put to you, he has the same duty to discharge in regard to the verification of the cash as he has with regard to the verification of the securities. However, gentlemen, to state the proposition is one thing, and to answer it is another, and I am very glad that the responsibility of answering it rests with you and not with me.

Now I have said, I think, all I think necessary to make it clear on the question I shall leave. Was the defendant, or were his clerks, guilty of any breach of duty or any want of reasonable care in the conduct of

their duty in the years 1900, 1901, 1902, or 1903, or, if so, in which of them? I tell you the Auditor is bound to take reasonable steps to see that any such important item as this is not inserted in the Balance Sheet without warranty, but what is the degree of the inquiry he ought to make must depend on the particular circumstances of the case. You will see the accounts and what was before him. While I tell you, on the one hand, he is not bound to suspect Mr. Frederick Clarke as being a dishonest man, he is entitled to rely upon the fact that he is the trusted official, and has known him for years, but that does not justify him not using reasonable precautions; he is not entitled to let his duty be performed on the credit of Mr. Frederick Clarke rather than perform his own duty upon his own responsibility. If you thought there was a breach of duty in one of those years, you would have an extremely difficult question to answer, and that is the damage caused. It may be a very substantial sum, of course. It cannot be more than £766, because that is the total amount of the loss; indeed, it cannot be as much as that, because I point out the Auditor does not guarantee the honesty of the employees. He could not do it, and, as Mr. Bankes properly put to you, if he ought to have found this out in 1898, as Mr. Bankes suggests, £133 *ex hypothesi* would then have gone, and that is the amount he suggested to you was not then forthcoming. If you take the view that that is not enough to show any want of reasonable care, the next year it had risen to £479, and if that £479 (I will take care that you have all these figures before you) had been by that time practically lost, Mr. Hasluck is not responsible for that. He is responsible for whatever damage you think has been occasioned by his not properly auditing the books.

Now to come to the really difficult question whether or not this money had substantially disappeared by the end of 1900. The only evidence we have got is the evidence of Mr. Hubble, and I quite agree with Mr. Bankes that he gave his evidence extremely fairly, as I think all the people in this case have done, notwithstanding the difference of position of some of them. Mr. Hubble does not say that he examined that cash box. There is a great deal that has been said on both sides, and I do not want to repeat what has been said by counsel on one side and the other most ably, but I think Mr. Isaacs gave you reasons for thinking that he asked for the amount without looking at it, and, remembering that Frederick Clarke was a secretive character, it may be that that cash box was not examined; but Mr. Hubble does say, "I certainly should not have made a requisition without seeing what cash I had in hand, because, though I knew what I wanted from the lighterman's estimate and from the wharf's estimate, there was something still I

wanted—namely, £20 or £25, as the case may be, and I should not have asked for it without knowing what it was.” He asked for three cheques—£85, £75, and £80. Gentlemen, you have to look, and I shall ask you to look, at that particular month, because I think, in justice to Mr. Hasluck, it ought to have been put. It is perfectly true that Mr. Hubble said he does not think all the credit entries in that year were entered up; he thinks some were, but naturally he cannot say what were entered up. If you look through that book there were very large balances indeed standing to the credit of this account all through that period from April 1900 to December 1900. If the book was at all made up at that time I cannot scarcely imagine Mr. Hubble’s attention not being called to it—that there was no less than £802 on the debit side and only £161 on the credit side, and at that time there was a balance due of something like between £500 and £600. If the book was not made up, and he had only to enter, as he did enter, the expenses as he paid them out, it would not convey the same indication to him as it does to us now. This is the difficulty of judging a case after the event. It is fair to Mr. Hasluck to say the condition of the book, whether it was at that time either not entered up, or, if entered up, showing a large balance in the hands of the cashier, does not appear to have excited the suspicion of Mr. Hubble at all. He makes no representation to his directors; he makes a request for very large cheques. It is a requisition on the 14th of December, £215; on the 21st December, £347; and on the 28th December, £200. Therefore he makes very large requisitions, and it is only fair to say, if the book was made up, that must have shown a very large balance in the hands of Mr. Frederick Clarke; and if the book was not made up, it would be a circumstance that Mr. Hubble would have called the attention of the directors to, but it does not appear to have excited his suspicions. You have this difficulty: Mr. Bankes suggests to you that practically the greater part of the money had gone by 1900, and that therefore, at any rate after that time £400 or £500 would have gone, there would not have been the further loss of £200 or £250; and I think you are entitled to take this view if he ought to have found out that there was this large sum supposed to be standing to the credit, which would have called the directors’ attention to it if the Auditor remarked upon it; then, though they would have lost that £400, they would not have lost the further sum, and the damages recoverable from this defendant would be something like £250. You have to consider, aye or no, did this failure of the Auditor to disclose it really cause the damage or not? You have to be satisfied that it was the result of the breach of duty. We do not know, unfortunately, what this man’s condition was; whether he was in money at one time of the year, and whether speculating or possessed

of money we know nothing about. The plaintiffs must satisfy you that the damage has been occasioned, to whatever extent you think it was occasioned, by the breach of duty on the part of the Auditor. If, although it was a breach of duty, this loss would have been sustained unless the man had stolen the money after the breach of duty was committed, of course you will find there was no substantial damage by this breach of duty. The action is for breach of duty, and the damage is nominal damages. I cannot give you much more assistance. I wish I could. On the one hand, it is said that £450 had gone by the end of 1900. If so, the damage would be somewhere about £300. If Mr. Isaacs is right in suggesting to you that the money may have been there on the 30th April 1902—not a very likely suggestion in view of what we know about the man, and the speculation was that the loss was due to improper conduct by this man, who was trusted and receiving large sums of money—whatever your views may be of the conduct of the defendant, you ought not to make him pay the damages, if he is not responsible. The conduct of the directors is no answer to any breach of duty by the defendant, but it is a circumstance you must take into consideration, because if you are of opinion that the loss was occasioned by the man stealing the money in consequence of there being a want of proper control over him, then the fact of there being a breach of duty by the Auditor is what we lawyers call a *causa causans*, which contributed to, but would not be the cause of, the loss. I do not know that I ever remember a question the solution of which was more difficult in the concrete. It is easy to put it in general terms: Was he guilty of breach of duty, and, if so, what loss was occasioned to this company by that breach of duty? You must not put upon him the loss by reason of theft occurring afterwards or before, but you must put upon him such damages as you consider in your opinion were really caused by his not having fulfilled his duty as Auditor of the company.

Now, gentlemen, I have endeavoured to put these questions clearly, and I will give you the papers in such a way that you can follow them, and then ask you to answer the questions. *That* is the list of balances; *there* are the Trial Balance Sheets; *that* is the actual Balance Sheet; and *this* is the demand that is made for the money each time. You will find the index number against each item, and will have no difficulty in tracing them.

The jury retired at 2.53.

The Lord Chief Justice: I did not refer to these conversations—the question about looking beyond one's nose and so on, because I thought they were so unimportant—but if you wish me to direct the jury upon them I will. The other is much more important.

Mr. Bankes : I am quite content, my Lord.

The jury returned into Court at 3.55. The foreman having handed up a paper to his Lordship,

The Associate : Gentlemen, are you all agreed?

The Foreman : Yes.

The Lord Chief Justice : As to the first, the jury say that there was a breach of duty in 1899, 1900, 1901, and 1902, and that there was damage to the extent of £5 5s. od. The jury add that they consider the directors have been guilty of gross negligence.

The jury was then discharged.

The Lord Chief Justice : I think this had better be mentioned to me to-morrow morning by Mr. Bankes and Mr. Isaacs. I think it is better that it should be, as they may have something to say—that is, mentioned either to-morrow morning or at any time convenient to Mr. Isaacs or Mr. Bankes.

Mr. Wallace : If your Lordship pleases.

JUDGMENT.

The Lord Chief Justice : As this case may go further, and I think it is a very important case, I should like to say in a few sentences why I cannot enter judgment for the defendant, and then I will deal with the question of costs.

There were two grave issues raised in this case. First, had there been a breach of duty or not? By "breach of duty" I mean a breach of contract. Had there been a breach of contract by the Auditor or his clerks? Mr. Hasluck, who is obviously a most honourable and straightforward man, elected to fight the case upon the basis that there had been no breach of duty. I was asked at the end of the plaintiffs' case to stop the case, but I felt that there was some evidence, especially as Mr. Bankes raised the point of there being circumstances which should have aroused the Auditor's suspicions, as to which I think there was no substantial evidence of any sort or kind, but still there was some evidence, and I could not stop the case. The defendant, in the course of his case, did not call the clerk by whom the audit had been conducted, and it seems to me under the circumstances, if my ruling was right as to the duty of the Auditor, it was quite open to the jury to find that they were not satisfied that there had been sufficient inquiry with regard to that particular asset in those four years, and I would call attention to the fact that the jury have, I think rightly, limited their finding to the years 1899, 1900, 1901, and 1902, when the asset was a substantial sum of money not less than £470 in the first year. I think

that there was a very substantial question of principle to be fought. It was not a case in which Mr. Hasluck had said (as he might have said quite honourably, I think): "My clerk was careless, but the directors so acted that it caused the company no damage." If that had been the way the case had been fought, I think Mr. Isaacs' contention would have been unanswerable, and that the action ought not to have been brought. I am bound to say I think that there was a very grave and substantial question to be fought and tried, which the jury have answered, in my opinion, absolutely rightly, that there was not a sufficient fulfilment of his duty in ascertaining whether that asset really existed. I particularly desire to avoid using the words "counting the cash." I do not think it is the true statement of the duty of an Auditor, although it is one way of putting it. Anything may be "counting cash," if you ascertain it is there; but, as I tried to point out to the jury, there may be cases in which the actual counting of the sovereigns is not even the best way of vouching or ascertaining the amount. Therefore I think the jury did take the view properly that there was not a proper discharge of his duty by his clerk—nothing morally wrong in the least, but not a sufficiently careful supervision by Mr. Hasluck's clerk of the asset which was believed to exist, and which was shown by the books to exist, because that the audit was most carefully performed I have not a shadow of doubt apart from this. I think there was a substantial issue properly raised by the plaintiff, and properly defended by Mr. Hasluck, if he determined to fight the battle on the ground he did fight it, that there was no duty on an Auditor to ascertain the existence of an asset, assuming the books showed that that asset ought to have been in existence. Therefore I think a substantial question had to be tried, and that entirely makes it impossible for me to say that there was not an issue before the jury as to breach of duty, and, if it was a breach of duty, at any rate there must be nominal damages.

Then Mr. Isaacs says because the jury have said the large damages found in the claim of the plaintiffs were not the result of that breach of duty (in which I absolutely and entirely agree) he ought to have judgment for the defendant. I only point out that that would have been a perfectly good argument had the defendant come into Court and said, "I do think my clerk was not sufficiently careful and did not sufficiently perform his duty, but no damage was caused to the plaintiffs." I do not think the defendant is entitled to have that issue tried and fought (and I need hardly say it was most ably fought) for the best part of two days at the plaintiffs' expense.

Then as to the costs, I confess I have very great doubt. In an ordinary case I do think the rule Mr. Isaacs indicated of letting the law

take its course is a very good one in actions of tort and libel, and cases of that kind. I think there was a substantial question to be fought here, and that the finding of the jury that the directors have been guilty of gross negligence, though a perfectly proper finding in order to show why they come to the conclusion that it was not the breach of duty which they had previously found that caused this large loss, ought not to affect the question of costs with regard to the trial of an issue of such very great importance to the parties, and in one sense probably important to the public, though I do not think that is important here, but it is a case in which Mr. Hasluck represents a great profession, and I therefore think that I ought to say this is a proper case to have been brought in the High Court, or whatever the form is.

Mr. Bankes: That there was sufficient reason for bringing the action in the High Court, my Lord.

The Lord Chief Justice: Yes. I give that certificate.

Mr. Bankes: And I ask for a certificate for a special jury.

The Lord Chief Justice: Certainly.

Mr. Rufus Isaacs: It is only a small question of costs left, but if I pay over those costs on the usual undertaking may I have a stay, my Lord?

The Lord Chief Justice: Yes; it is clearly a case in which you are entitled to carefully consider what I said to the jury.

Mr. Rufus Isaacs: I do not say I shall want to, but I want to consider it before we go further, my Lord.

The Lord Chief Justice: I know the difficulties, and the extreme possibility that one may not go right, especially at *Nisi Prius*, and I am sure in a case of this kind you might pay over with the usual undertaking, if necessary.

Mr. Rufus Isaacs: I understand that my learned friend prefers the costs should be paid into Court.

The Lord Chief Justice: So be it.

Mr. Rufus Isaacs: Then there will be a stay till taxation.

The Lord Chief Justice: For a fortnight. I suppose if it is brought into Court you do not want a stay.

Mr. Rufus Isaacs: Yes, because we cannot bring it in until taxation. It is only a question of the form of the order.

The Lord Chief Justice: There will be no difficulty with the plaintiff company, I am sure, as to that.

(*Acct. L.R.*, XXXI., p. 1.)

The case of SMITH v. SHEARD.

(Decided before BRAY, J., and a Special Jury, at the Liverpool Assizes, on May 9, 10, and 11, 1906.)

Liability of Accountant—Audit at request of Creditors—Defalcations by Employee—Claim for Damages.

An action was brought by Mary Ann Smith, married woman, carrying on business as a manufacturing stationer in Liverpool under the style of Dickinson & Co., for damages for neglect in the audit of her books, against Theodore S. Sheard, accountant.

Mr. Rutledge stated that the plaintiff claimed damages for neglect and carelessness in the audit of her books, by means of which she incurred heavy losses consequent on frauds. The defendant denied that he was the Auditor of her books, and that she sustained any loss through neglect on his part, and also that, if there was neglect, the plaintiff was guilty of contributory negligence; while further, the defendant counter-claimed for certain sums for work done, which plaintiff denied.

Mr. Shee, in his opening, stated that the allegation of neglect was that in consequence of the inefficient auditing of the books by the defendant, the late cashier of the plaintiff embezzled certain sums of money, amounting in all to about £700. Plaintiff had been in partnership with Mr. Dickinson, but on account of the latter overdrawing more than he was entitled to this partnership was dissolved in 1902, and a consultation with the creditors was decided upon. Mrs. Smith then found that Mr. Sheard had been acting as Auditor to the firm, and she intimated that his services would be continued in this capacity. As a matter of fact, it was alleged that he not only undertook the auditing, but her affairs in regard to the creditors and the collection of debts. In December 1902 the plaintiff's cashier, who had since been prosecuted and who was now dead, began to make fictitious entries in the books and appropriate money from the business. When defendant audited the books and prepared a Balance Sheet in 1904 he made a charge of forty guineas, to which plaintiff demurred, remarking that she did not think the work had been done properly. Mr. Sheard replied that the consequence of such a statement would be very serious for one of them. The defalcations of the cashier were not discovered until April 1905, and it was contended that if the audit had been an efficient and proper one the misappropriations would have been found out much earlier, and the losses thus prevented.

Evidence was given in support of counsel's statement by the plaintiff.

Cross-examined by Mr. Horridge, witness stated that in order to save expense, and because of the confidence she reposed in the cashier, she did not instruct the defendant to audit her books in the way he had done in the time of Mr. Dickinson, and that consequently the Bank Book, Cash Book, and vouchers were not examined for eighteen months.

Miss Amery, in explaining the system of bookkeeping at the plaintiff's office, stated that the defaulting cashier collected accounts outside and gave receipts from a counterfoil Receipt Book, which she was unable to say was asked for by the defendant's representatives.

Cross-examined, witness said that everything was left by Mrs. Smith to the cashier. As far as she knew, Mr. Sheard never had the Counterfoil Book, the rough Cash Book, or the vouchers.

Walter Appleton, of London, representing a firm of creditors, stated that at a meeting of the creditors when Mrs. Smith took over the business it was agreed to give the plaintiff time to pay the debts on condition that Mr. Fosbrooke, the defendant's partner, took entire control of the books.

Arthur Whittaker, Chartered Accountant, Manchester, deposed as to the state of plaintiff's account books and the evidences of the partial audit which they bore. The question of what an audit was was a difficult one, but a generally accepted opinion was that it meant a comprehensive investigation of the books for the verification of the entries in order to arrive at a proper statement of the position of the client. He did not think there was any difference between an audit and a "complete audit," and without some understanding to the contrary an auditor must audit all the books. He maintained that the entries from the rough Cash Book into the general Cash Book, and from the original carbon counterfoils to the Summary Book, had not been checked as they should have been. Vouchers also should be asked for by an Auditor.

Mr. Horridge said he did not dispute witness's evidence as to non-checking, the whole point being as to what were the terms of defendant's employment.

The question of amount, it was agreed between the parties, should be reserved for the present.

Witness, proceeding, stated that if vouchers had been asked for fictitious entries would have been discovered in the Cash and Purchase Invoice Books.

Cross-examined by Mr. Horridge, witness stated that his evidence had been given on the assumption that the defendant was employed to give an audit in the strict sense of the term. It was apparent in this case from the books that the defendant had not purported to audit in such a manner as to check the honesty of the servants. It was usual for an Auditor to certify the accounts as "audited and found correct." Mr. Sheard had not done this. There was no necessity to ask for the counterfoils of receipts for the purpose of posting the books and preparing a Balance Sheet only.

Two other witnesses were called for the plaintiff, whose case was then concluded.

Mr. Horridge, for the defence, argued that from the very first Mr. Sheard had taken up the position that he was never engaged to audit, and that he had never for one moment pretended to do so. He had only done the work of checking the books and making out a Balance Sheet in a way that was the custom amongst private firms. It was not intended to audit the books to check the accuracy of the entries or the honesty of the servants, but simply to take out a Balance Sheet which correctly represented the books. That was shown by the very fact that the defendant had never asked for vouchers and counterfoils. The arrangement when the partnership between Mrs. Smith and Mr. Dickinson was dissolved was that the books should be put on a proper system of double-entry, and balanced half-yearly. Mrs. Smith did not want her cashier checked, as she reposed the fullest confidence in him. He maintained that if the word "audit" had not crept loosely into a bill that action would never have been heard of. Mrs. Smith had constantly stated that she wished to save expense, and she intimated that it was only necessary to do sufficient to satisfy the creditors by putting the books on a better system and furnishing a Balance Sheet. Counsel proceeded to quote letters bearing on Mr. Sheard's engagement, and submitted that every document and inference was in favour of the defendant. The secret of that case was that Mrs. Smith had lost her money through her late cashier, and that she never made a bargain with Sheard to audit at all. The Balance Sheets were not signed or certified for the simple reason that an audit had not been made or had been intended to be made.

Mr. T. S. Sheard, the defendant, gave evidence. He said he had carried on business in Liverpool as a Chartered Accountant for twenty years. He emphatically denied that he had ever agreed to make a complete audit of the plaintiff's books or anything to that effect. If he audited accounts or Balance Sheets he usually gave a special certificate stating what he had done. If he was only instructed to take out a

Balance Sheet he took the figures as stated in the books, and did not sign it.

Cross-examined, witness disputed that there was any discussion between himself and Mrs. Smith about it being a serious thing for her if her statement about his work were false. He was astonished when he was blamed for the non-discovery of the defalcations.

John D. Fosbrooke, defendant's partner, stated that in consequence of Mrs. Smith's anxiety to save expense until the creditors had been paid off, the arrangement was that he should only check the posting in order to enable him to balance. He denied that he had told Mrs. Smith that he had made a "complete audit" of her books. The word "audit" had been put into the bill of charges by a clerk, and it should have been "auditing of posting." He did not ask for vouchers, because he was not making a thorough audit of the books.

Cross-examined by Mr. Shee, witness stated that it might have been less trouble if he had let the cashier do the posting, and if he (witness) had applied himself to checking the cashier's honesty, but witness was stopped by Mrs. Smith from doing that.

Mr. Sidney S. Dawson and Mr. W. C. Spencer, Chartered Accountants, deposed that it was the practice after making a thorough audit to sign the Balance Sheet or give a certificate. In this case, Mr. Spencer said, there was no evidence of vouchers, &c., having been checked. The work done by the defendant was not valueless, but was necessary for balancing purposes, and in the absence of fraud would have shown the assets, liabilities, capital, profits, and drawings of the partners.

In answer to Mr. Shee, witness said that the defendant's audit would be valueless for the purpose of detecting fraud.

Counsel having addressed the jury,

Mr. Justice Bray, in summing up, said: Gentlemen of the jury, I may have to occupy your time for a little in going into this matter, which is a very important matter. It is important for both parties; it is important for the plaintiff because she says that Mr. Shand has defrauded her of some £700, and that if the defendants had done their duty Mr. Shand would have been detected long before all that money was lost and she never would have lost the money. £700, of course, is an important sum. On the other hand, it is equally important for the defendant—not more important, but equally important for the defendant—not only because the sum is a very considerable sum, but because he is charged with having entered into a contract which he never performed or attempted to perform—that is the charge against him. It is a serious charge against professional men, and when Mr. Shee talks

to you about disregarding the question of onus of proof, and asks you to look upon it as a matter of common sense, I ask you to look upon it as a matter of common sense. First of all, at law common sense and law usually agree, but it is law that the plaintiff must make out a contract, and a breach of that contract before she can succeed. But it is common sense too. One of you gentlemen some day might be sued by somebody setting up some verbal contract which you have never entered into, and you would think if an action were being brought against you—would not you think it was fair that when there are no documents proving what the contract was, if there are no documents it is a case that should be proved against you fully? Now the law says that, and common sense tells you the same. Now, gentlemen, as I have told you, this is an action for breach of contract, and it is admitted that the whole question turns upon what was the contract, and therefore the simple question that I am going to leave to you is this: Did the defendants agree with the plaintiff to make her a complete audit? Is that what they agreed to do? That is what the plaintiff has got to prove to you, because it is common ground that if that was their contract they never performed it or attempted to perform it; because it is common ground again that a complete audit means having every item vouched for and every entry—every book brought up and every item vouched for—and, of course, it is common ground again that if every item had been asked to be vouched for and every book had been examined the defalcations would have been discovered; they must have been discovered. Therefore that is the question that you have got to try. Has the plaintiff proved to your satisfaction that the defendants agreed to make a complete audit? Now it is purely a question for you; it is not for me, it is for you; and any observations that I may make, except when I am dealing with a question of law, are observations which you can give just as much or as little weight to as you choose. Now I am bound to say that the first observation which occurs to me is this: It does seem to me a remarkable thing that if these people really did agree to make a complete audit that they should not have done it. It was to their interest to do it. There was no bargain as to price, and the more time they had to spend upon these books the more remuneration they would get, and you, gentlemen, know, of course, there is a profit upon every hour's charge that they make, and it was to their interest—to their profit—that they should make as complete an audit as possible, because that would take more hours and would mean more profit, and it does occur to me that that wants explanation, why the defendants if they had agreed to make this complete audit never did so. Now, gentlemen, that is an observation on the law; it is simply an observation that you will take notice of. Now, as I told you, the

plaintiff has got to prove her contract. The contract, whatever it was, was clearly made about the beginning of 1903; that is common ground. Whether it was in December or January does not much matter; the defendants put it in January; the plaintiff does not give any actual time herself, except that it was about that time. Now first of all you have got to see what did the plaintiff say herself, and you have got to ask yourselves, is that true? If it is true, what does it mean? Or if it is not true, what was the contract? Now this is what she said: "Fosbrooke was Sheard's general manager, and he asked me what I was going to do about the audit. I told him I was going to make no change in anything." Now that is her own story, mind you, the story that she repeated more than once, which means, if one can understand it, it means you are to go on doing the work which you did before. Then she says: "I told him I was not going to make any change in anything, and knowing I had no knowledge of books I expected them to do all my books. I am not sure of the words I used. I said I hoped they would take special care, knowing that I knew nothing about books, and I was making no change at all. Fosbrooke told me he was going to take special care about the books, and he should want to make a few alterations. Mr. Shand was my head man; he was called in, and I told him to give every assistance to Mr. Fosbrooke." Now she is cross-examined, and Mr. Horridge wanted to see whether he was quite clear that he understood the contract—that according to her version they were to do what they had been doing before. The employment was the same, but they were to take more care. What I do not understand—the employment was continuous—they were to audit the books in Dickinson's time, but they told me they could not get at them. Now, gentlemen, of course that is her story. Now let us see what the contract was that was made. You have got to look at what had happened before, and therefore it is most vital to see what was the work they had been employed to do before. Now I must go right through that with you, but there cannot be a shadow of doubt, although it is for you to say that they were never employed to audit the books before and never did so. Now you will see. You know bills were sent in. According to Mr. Fosbrooke these bills were brought to the plaintiff—to Mrs. Smith—when she was making the arrangements for going on with the work at the time this contract was made in January 1903. Now the correspondence shows this, that the first time these defendants were employed by the firm of Dickinson & Co. was about March 1900, and they were employed for this reason. Mr. Dickinson—I suppose their position perhaps was a little critical—Mr. Dickinson wanted to know first of all what were the total annual sales; he wanted, secondly, the Balance Sheet made up to the end of the 31st of January 1898, so as to show what was the

position between them as to capital. Apparently their arrangements were more or less vague as to capital, and they wanted to commence and see how much capital Mr. Dickinson had got in the business, and how much Mrs. Smith had got in it. That was the object with which they were employed. Now you get from the documents and from Mr. Sheard's evidence—not denied by Mrs. Smith—the common question. Now Mrs. Smith tells you, "Oh, I knew nothing of what was going on in Dickinson's time." Now we shall see that is not quite correct. She knew; she wanted to know as much as Mr. Dickinson where they were as to capital. Now we will see from the bills that were sent in what they were doing. Now, gentlemen, I will hand in the bills to you, so that you may follow them. I think the first of them—it is not here—gentlemen, you take those (bills handed to the jury). The first one is not here. I will give it to you presently. "28th May 1901. For services rendered preparing schedule showing the total sales of your business from April 1898 to April 1900." You won't find that one here; I will hand it to you. "Preparing Balance Sheets at 31st December 1898 and 31st March 1900, and Profit and Loss Account for the eighteen months ending 31st March 1900, £42." Now you take that. Now I have read it to you it is perfectly clear from that that there was no audit; there is no pretence for saying that there was anything in the nature of an audit. Now the next is this. You have got the next one yourselves. It is No. 2. You will find these later ones are all misleading—the 31st January 1903—because they were not delivered until that time. "31st January 1903.—For services examining and balancing your Cash Book for the year ended 31st March 1901." Now again it is agreed that is not audit. Mr. Shee does not suggest that is audit. "Checking Ledger balances and preparing Balance Sheet at that date. Attending numerous interviews with Mr. Dickinson and Mrs. Smith, discussing affairs, and reporting as to cash drawings monthly, fifteen guineas." You know Mr. Sheard says it is quite plain from the correspondence that they discovered when they got out these Balance Sheets that Mr. Dickinson was apparently overdrawing, or drawing more than he should do, and was making the capital too small, and the result of what took place appears from a letter of May the 1st 1901, and that is a letter from Mr. Sheard after he had seen Mr. Dickinson and Mrs. Smith. "In confirmation of my interview with Mr. Dickinson and Mrs. Smith on Monday morning, I beg to recapitulate the arrangements that were then come to." Now you know Mrs. Smith talks a little about her knowing nothing of what was going on. She and Mr. Dickinson had met and had arranged what should be done. "(1) The Balance Sheet as at 31st December 1898 is to be taken as a basis of the partnership agreement, in accordance with which the capital therein shown is to be apportioned

two-thirds to Mr. Dickinson and one-third to Mrs. Smith." Then Mr. Sheard had written some five days before that pointing out quite clearly that that Balance Sheet did not profess to be an audited Balance Sheet. The parties agreed that that should be so. "(2) Balance Sheet made out as at 31st March 1900, and the profit thereby shown for the previous fifteen months is also to be taken as correct. I am to proceed." Now this is what he had to do: "As quickly as possible to prepare a Balance Sheet as at 31st March 1901, and on the completion of same a further meeting will be held, when it will be decided whether such Balance Sheet should be adopted as correct. (4) From the 31st March 1901 the books are to be placed upon a proper system of double entry and balanced half-yearly. In future a rough Cash Book is to be kept, into which are to be entered full particulars of all payments and receipts, and the balance in hand is to be paid into the bank daily. With a view to carrying out the foregoing arrangements Mr. Fosbrooke yesterday interviewed Mr. Shand and discussed the future bookkeeping. I find several alterations in the system of bookkeeping will be necessary, as many of the present methods might be improved upon." There is something about Purchases, about Sales, about Allowances and Returns, and about Ledgers, and so on. I need not read that all to you. It points out the alterations that Mr. Sheard is going to instruct Mr. Shand to carry out so that the books may be properly entered up with double entry, so that he may be able to make Balance Sheets. Now the next thing that happens is this: There was a number of accounts owing, it being found that Mr. Dickinson was drawing all the money from Mrs. Smith's balance. There was sent an account of the drawings—the monthly drawings—and this is the form of that: "Dear Sir,—I beg to report that I have examined your Cash Book for the months of June and July, and that I find the drawings are as follows:—Mr. Dickinson so much, Mrs. Smith so much. I have also to report that the following cheques appear in the Bank Book, but are not entered in the Cash Book, and that a corresponding number of counterfoils in the Cheque Book are blank." Then follows a list of these items, and "Please let me know to what account these are to be debited, and oblige." Now that was the usual form, and that went on until September—about the middle of September 1902—when Mr. Dickinson left the office, and then the question arose, What was to be done? Mrs. Smith took the advice of a solicitor. She took advice, and the advice was to get rid of Mr. Dickinson, and accordingly that was done. Then, unfortunately, there were creditors who were pressing. What was to be done? The creditors had to be asked for time. The principal creditors were asked for time, and the proposal was that they should take bills for four, eight, and twelve months, so as to give Mrs. Smith time to turn round. Now we

follow the accounts. The accounts say what work was done with reference to that. The next one we have got is 1901 to 1902. That is No. 3. I think, "For services examining and balancing your Cash Book for the year ended 31st March 1901, checking Ledger balances, and preparing Balance Sheet at that date. Attending numerous interviews with Mr. Dickinson, Mrs. Smith, and Mr. Wilson"—Mr. Wilson was Mrs. Smith's solicitor—"discussing affairs, and reporting monthly as to cash drawings, fifteen guineas." The next one is headed 1902, "For services examining and balancing your Cash Book for the nine months ended 31st December 1902, extracting Ledger balances, and preparing Balance Sheet at that date. Attending numerous interviews with Mr. Dickinson, Mrs. Smith, Mr. Wilson, and Mr. Duncan; discussing affairs and reporting as to cash drawings, fifteen guineas." Now it is quite clear that up to that time their work did not consist of auditing; it consisted of examining and balancing the Cash Book, and ascertaining the cash drawings of the different partners, and preparing Balance Sheets, and I think in some cases the Profit and Loss—no, I think there was no Profit and Loss—preparing Balance Sheets, so that up to that time it is common ground, and it really cannot be disputed, and up to that time nothing had been done in the way of auditing. Now let me read again. That being so I ought perhaps to follow these up a little more. You know there was to be a meeting of creditors, and there was a meeting of creditors on the 22nd December. Now what took place at that time appears from the letter of the 24th of December, which was Mr. Fosbrooke's letter: "In reply to your letter of the 23rd I am pleased to hear"—Oh, this is a sort of circular letter sent, or at all events sent to one of the creditors, it may be to more. "In reply to your letter of the 23rd I am pleased to hear that you will agree to the agreement," and so on. "Mrs. Smith wishes me to thank you on her behalf. Mrs. Smith regrets that she cannot send you cash for the dishonoured bill (£133 4s. od.), as she must treat all creditors alike. I may also inform you that Messrs. Fenner Appleton & Co.'s account is not only for a larger amount than yours, but it dates back three months earlier. Mrs. Smith proposes to take stock during the holidays, and I will then prepare a Balance Sheet made up to date, and submit it to you and the other creditors at another meeting in London early in the new year, when final arrangements can be made. In the meantime Mrs. Smith will pay you cash for any goods she may require." So that it is quite clear that at the meeting of the 7th there was no final arrangement. The creditors wanted, before they had a final arrangement, to see a Balance Sheet which Mr. Sheard was to prepare. He did prepare that Balance Sheet, and the meeting was held on the 21st January, and attended by Mr. Sheard, not by Mr. Fosbrooke, because Mr. Fosbrooke

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was ill. Now then we will see what happened then, because there are letters which are relied upon by both parties. Now on the 23rd January Mr. Sheard sent round to these four principal creditors a circular letter. Now this is what is relied upon by Mr. Shee. "Since I had the pleasure of meeting you in London on the 21st instant I have seen Mrs. Smith, and she agrees to your suggestion that she should give you bills at four, eight, and twelve months from the 1st January instant for three equal instalments of your debt. She is also prepared to give an undertaking not to draw more than £2 10s. od. per week for herself until all these bills are met. She further agrees that I shall at the end of June next audit her books and report the result of my investigations direct to you. Will you draw upon her as above, or do you wish me to draw out the bills? Your kind reply will oblige." Now Mr. Sheard undoubtedly uses the word there, "Audit her books." Now what did that mean? There is an answer to that letter. The creditors, or one person on behalf of the creditors, Messrs. Fenner Appleton & Co.—that is the gentleman you saw—he answers that, and you will see how he construes it. "In reply to your favour we enclose bills at four, eight, and twelve months for the amount due to us up to December 31st last, which please get accepted and return to us. We agree to take a settlement of our account by means of these bills, solely upon the following conditions, and on the understanding that if they are not all fulfilled, or if there is a failure on the part of Messrs. Dickinson & Co. to meet any of these bills at maturity, then the whole of the unpaid portion of the debt becomes immediately due. The conditions are that Messrs. A. Cowan & Sons, Lim., Dickinson & Co., Lim., and Spicer Bros., Lim., agree to accept payment of their accounts on the same basis, and that Mrs. Smith does not draw for her own use more than £2 10s. od. per week until the bills are paid, and that you furnish us with a Balance Sheet every six months until the bills are paid." Now you see he does not use the word "audit," but says "furnish us with a Balance Sheet." That is his interpretation of the condition which was made. He said in his evidence that what was said was that Mr. Sheard should have full control over all the books. Well, I do not see how that can mean an audit—"complete control over all the books." It means they should have the direction of how the books should be kept. At all events, there is no word of an audit in that. Now that is how the matter stood, and, as I say, it is common ground that up to that date there had never been an audit by Mr. Sheard in the strict sense of the word, and all they had done was to go into the cash balance for the purpose of the drawings and to make out Balance Sheets. Now, that being so, you have to ask yourselves, What does this mean? and I am taking the plaintiff's version as true. You know the defendant and Mr.

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Fosbrooke deny it, but I am taking the plaintiff's version: "He asked me what I was going to do about the audit. I told him I was going to make no change in anything. I said, 'They know I have no knowledge of books; I expect them to do all my books.' I cannot be sure of the words I used. I said I hoped they would take special care, knowing that I knew nothing about the books, and I was going to make no change at all." Now you know Mr. Shee has put it to you. He says that is all very well, but this was a poor woman, and it was the duty of the Auditors to make it plain to the poor woman, but that is not so. If the Auditors directly deceived her that would be one thing. It is not their duty. She was telling them—instructing them—what they should do. It is her duty to make it plain to them what they were to do, not his duty, and I must tell you that Mr. Shee's suggestion that it was the duty of the Auditors to make it perfectly plain what they were going to do, and what they were not going to do, was not good law; and it is not good sense, gentlemen. Mr. Shee talks about a poor woman, but you must recollect that this is a lady who has been carrying on this business and managing part of it, and if women go into business they must be treated as business people; many of them are more capable than men to understand business matters, but they cannot come before you being business people in this way and say, "Oh, I knew nothing; it was the duty of the Auditors to make it plain to me." She was giving them instructions what to do; it is for her to show what she instructed them to do and what they agreed to do. Now you must take that from me, and you must take it from me that Mr. Shee's observations on that point are not good law. She has got to make out what the contract was. Of course, if they intentionally mislead her that would be another matter altogether, but now look what it was. They were Auditors. They wanted to be employed. Naturally their wish would be to be employed to do as much work as possible, but they have no right to do more work than their contract instructed them to do, and if they come here and ask to be paid for a complete audit Mrs. Smith would say, "I never asked you to make a complete audit. I asked you to take special care of the books." That is quite true. They were to give very careful instructions how the books were to be kept, and Mr. Shand was sent in for that very purpose. Now you have to take the contract as alleged by Mr. Fosbrooke, because he was the person who attended the interview, and it is he whose evidence you have to consider rather than Mr. Sheard's. Mr. Fosbrooke said, "We had done no auditing up to that point at all. I had not attended myself the January meeting, but I went there with these accounts, and then the question arose what was to be done. There were no instructions to me to do anything more than this Balance Sheet

which I had been instructed to do, and the creditors required me to do, but it was discussed what should be done and what postings I should check and what I should not. To begin with, I said 'There are a number of old accounts due. They ought to be collected by Mr. Shand. It will take a great deal of his time; you had better get him an assistant bookkeeper,' and accordingly Mr. Fosbrooke arranged what Mr. Shand should do in the way of checking and posting, and what this lady—she was not called in until some time afterwards—what she should do, and not a word was said about auditing at all." Now, as I say, you have got to ask yourselves first of all, does the plaintiff make any case upon her statement? If she does, is she telling the truth, or is Mr. Fosbrooke telling the truth? You know what happened afterwards. We know that from that time right up to August 1904 they did not attempt to make a complete audit. How is that to be accounted for? If they were instructed—Mr. Shand was there—Mr. Shand was present at this conversation apparently, or the early part of it—how was it that no remonstrance was ever made to them for not having done the audit? Of course, it may be said that Mr. Shand was going to swindle Mrs. Smith, and therefore it was not to his interest to do so, but certain it is that they have never attempted to do the work of auditing. Mr. Whittaker pointed out a number of things that they did not do. They never asked for the counterfoil Receipt Book, or for the rough Cash Book, to compare it with the Cash Book, or that a single item should be vouched from beginning to end, which is important. Of course, you have to consider the question of the honesty or dishonesty of Mr. Shand. Now, again, you have to look, according to Mr. Fosbrooke, who said Mrs. Smith pointed out again and again to him that she wanted the expense brought down as much as possible. Could not Mr. Shand do this, and could not Mr. Shand do that, and it was arranged that Mr. Shand should do this and that—certain things to save time and money. Does that seem reasonable, to say that Mrs. Smith was a reasonable woman? They never dreamt of Mr. Shand being dishonest. He had been in their service some time, and it was never dreamt of. All that she wanted was such a Balance Sheet as would satisfy the creditors, and they were not going to be satisfied with Shand's Balance Sheet, and they got an accountant's Balance Sheet. That was the object of the employment. That went on apparently without much important happening until July 1904. Now apparently they had no instructions to go beyond the second Balance Sheet. The creditors were paid off by the end of March 1904. The creditors were paid off, and therefore there was no necessity, as far as the creditors go, to have the expense of any further Balance Sheet, and now come some very important matters about this month. Now the first thing is letters that have passed of

July 1904. Now it is exceedingly difficult to understand what these letters were. One must remember that at this time Mr. Shand—the writer of these letters—had commenced his defalcations, and they had been going on for some months—they had begun, I think, about a year before this, and apparently it is common ground. Mr. Fosbrooke had told Mrs. Smith that he had noticed that Shand smelt of drink, and therefore there might have been a little friction, and apparently there was some accountant whom Mr. Shand rather wanted to be brought in. Now this is written by Mr. Shand: “We must ask you to push on with our Balance Sheet to March 31st 1904. The original arrangement with you was that the Cash and Bank Books were to be balanced and audited monthly. We should be pleased if you will see that this arrangement is carried out in the future.” Now that is not an audit at all. It was the Cash Book and the Bank Books that were to be compared. “The original arrangement with you was that the Cash and Bank Books were to be balanced and audited monthly. We should be pleased if you will see that this arrangement is carried out in the future.” Now that arrangement had been made in Dickinson’s time, and was utterly absurd now—utterly absurd. Now this is Mr. Sheard’s answer: “In reply to your letter of the 15th inst., I am proceeding with the Balance Sheet to March 31st, and hope to hand you the result shortly. I should have completed my work before now if there had not been so many errors, discrepancies, and omissions in the books, and in any case I am informed that the stock will not be ready until next Wednesday, so that it would have been impossible to complete the Balance Sheet earlier. I note that you wish the Cash and Bank Books to be audited and balanced monthly, which shall have attention, but this is the first intimation I have had that you wished the arrangement which was made in Mr. Dickinson’s time to be carried out after his retirement. Of course, to do this it will be necessary for the Cash Book to be written up and balanced monthly, which has not been done in the past.” Now there was no answer to that. The defendants rely upon that as showing that this was an intimation that there was no complete audit going on. Well, it is very difficult to see whether what they were complaining of was that they had not been done monthly, or that they had not been done at all. It is very difficult to understand those words. The next is August 16th: “Dear Sirs,—I beg to advise you that I have got out a Trial Balance to 31st March of your books, and that they do not balance by the sum of £19 15s. 6d.” That is a Trial Balance Sheet. I daresay, gentlemen, you know it is the first attempt at a Balance Sheet that is given. “As the books have not been kept in the manner I instructed, and as I have had to make a number of entries to balance accounts ruled off in error as settled, it appears to me that it will take

a considerable time to find the errors and balance the books. I have already discovered nearly 100 single entries and mistakes amounting to £70. I shall be glad of instructions as to whether you wish me to balance the books or to write the amounts off." Now what Mr. Fosbrooke says to that is, "If I had been an Auditor that would have been a perfectly ridiculous letter for me to write, because if I was an Auditor I would have to go through every figure. If, on the other hand, my object was to make a Balance Sheet, why first it was for my employer to say whether I ought to clear up this discrepancy of £19 15s. 6d." Now what do they say? Of course, it might be said they ought to have said: Why, you have got to audit, and if you have got to audit there cannot be any letters of credit. You must audit and find the actual figures. Then the next letter is: "We are in receipt of your letter of the 16th inst., and note that you are unable to balance our books by the sum of £19 15s. 6d., and to save further expense you had better write the amount off." Now that is relied upon very strongly by the defendants as showing Mrs. Smith's object was at that time to save expense as much as possible. She wanted to have a Balance Sheet which would show her position, but it did not matter to her whether it was £50 one way or the other. Well, then, the letter goes on and disputes the suggestion of Mr. Sheard that they had been making errors and mistakes in their books. They say they have not. They say they have been doing nothing of the sort. "We believe there is a balance due to you, and will feel obliged if you will send in a statement of particulars to enable us to arrive at a settlement, after which we can go into the matter of fresh terms." That means the fresh terms will settle up for the old. We will then consider whether we shall employ you or not to go into the accounts of the 31st March 1905. Now on the 19th, and before the Balance Sheet comes, there is an interview, and at that interview there is a conversation, as to which the parties do not differ very much. It is quite clear it did take place. On the 19th, before the accounts had been sent out, in which Mrs. Smith asked, "What is the amount; what are you going to charge me?" and he said, "Well, if I charge according to the hours employed it will come to something like 60 guineas." "Oh," said she, "that is a great deal too much," and he said "Perhaps it is too much. I shall charge you 40 guineas." "Oh," she said, "that is too much," and he said "Oh, well, I cannot reduce it to less without seeing Mr. Sheard." They both agree that that took place about that time, and it is fairly common ground that that took place. And, further, this took place: Mrs. Smith says herself, "I have asked him the terms for a perfect audit." Now the letter goes on: "As stated in our interview yesterday, I shall be pleased to undertake the complete audit of your books, and to furnish you with a Profit and

Loss Account and Balance Sheet annually for the future at the following fees, provided the bookkeeping is carried out under my supervision and according to my instructions: If one set of books is kept, 30 guineas per annum; if two sets of books are kept, 40 guineas per annum. These amounts would also cover the cost of checking the Cash Book and Bank Book monthly, if you wish it done." Now, gentlemen, there was no answer to that, or the only answer was— Yes, there was an answer: "We are in receipt of our Balance Sheet to March 31st 1904, together with your letter, which will have our attention in the course of a few days. Your bill of costs for periods ended 30th June 1903 and 31st March 1904 we consider excessive, and our Mr. Shand will see you on this matter, after which we can go into the matter of future charges." Now, gentlemen, it is a remarkable fact that the defendants never were employed after that to go into the matter. Now that seems of importance. You know if Mrs. Smith was so anxious to see whether her servants were being honest or dishonest there was exactly the same necessity for a full and complete audit then as at any time. Instead of that she never makes any reply to that letter, and never employs the defendants again until after Shand's defalcations are discovered, so that Mrs. Smith—who was so eager, as suggested, to have everything and a complete audit made—had no audit, no Balance Sheet, or anything during that time until Shand's defalcations were discovered. Of course, she had had a Balance Sheet up to a certain time because of the creditors. As soon as that was removed she does not seem to have wanted anything at all. You must ask yourselves how does that bear upon the case. Does that look as if she wanted to spend as much money, or to spend a considerable amount of money, in Balance Sheets and auditing and complete auditing or not? Now the next thing that happens after these orders is a suggested interview, at which Mr. Sheard is present and not Mr. Fosbrooke, when Mr. Sheard presented his accounts and required payment. The accounts, by-the-by, were sent on the 20th August, and were acknowledged on the 22nd, when Mr. Sheard was present. Now it does not seem to me that that is an interview of much importance. It took place afterwards. It took place after all the work had been done, and now they have no effect one way or the other upon it. Mrs. Smith's version, corroborated by the bookkeeper, is this, that she said, "Mr. Shand tells me you have not done your work properly," and that Mr. Sheard said, "That is a very serious thing. If it is true, it is a serious thing for my clerks. If it is false, it is a serious thing for you. Be good enough to put your complaint in writing." "Yes, I will," says Mrs. Smith. Those are Mrs. Smith's own words, "And I told Shand to do it." But it is quite clear that Shand never did do it. It was upon that that Mr. Shee put in letters of August 16th and

August 17th, as if that would affect it, but that will not do. The accounts had not been delivered at that time, and it is quite clear that that interview must have taken place a great deal later than August, when they were pressing for payment. Now these accounts were sent in. Now we must come to these accounts, because it is on these accounts that the plaintiff lays the greatest reliance, and there is no doubt that that account uses the word "audit." There is no doubt about it. Now it is said that the word was used in a loose sense, and they must have known perfectly well. They said: "We have never been pretending to audit in the full sense of the word"; but there it is, and it is a fact in favour of the plaintiff as against the defendants. It is a great point made by Mr. Shee, and you must form your own opinion upon it. Is it an admission that they had agreed to make a complete audit of the books, and had not done so, or is it a loose expression just saying what they have done? "For services opening books at 1st January 1903; auditing same for six months ended 30th June 1903; preparing Profit and Loss Account and Balance Sheet at that date, and writing up Private Ledger, £21." That is for the first six months. The next is, "Auditing the books for the nine months ended 31st March 1904; preparing Profit and Loss Account at that date and Balance Sheet at that date, and writing up Private Ledger, £21." Now, what Mr. Horridge says as to that is that they used a loose expression, and that is the whole origin of this action. She consulted accountants and other people, and they said, "You have got a case, because in their own bill they put down 'audit.'" Now you have to decide. You have heard Mr. Horridge upon it, and you have heard Mr. Shee. That is the matter. It is not the contract; it does not pretend to be the contract. You have to see what the contract was that was made in January 1903, and by looking properly at all the correspondence, and certainly at these accounts, you see what they agreed to do. Well, they squabbled for some time about these accounts, and so on. There are several letters about mistakes on one side and the other, and so on. Apparently Mrs. Smith was dissatisfied, and it was quite plain she was dissatisfied with these bills, and that they were too much; and observe that at this time Mrs. Smith, according to her story, knew that the defendants had not done their duty. Now what does she do? She gives bills in January 1905—gives two bills, one payable in May and the other payable, I think, in September, and when the May bill becomes due she asks that it may be renewed. It is renewed, and she pays it, and it is only when proceedings are threatened upon the second, which became due in September, that then she formulated, so to speak, the counterclaim which she has brought. Now the discrepancies were found out. The defalcations were found

out in April 1905. Now Mrs. Smith, according to herself, then knew how badly she had been treated apparently by the defendants, and what does she do? Who does she employ—who does she employ to make out the accounts to show these defalcations? She employs the defendants again for that purpose, and you have to ask yourselves what light that throws upon it. According to her she knew that her audit had not been properly done, and that she had suffered by it, and she employed the very people again, and she never formulated a claim against them by any writing so far as we have got. If she is right and she has got a good cause of action against them, she never does that until they press her for the £21 in October, several months afterwards. She said, "Oh, the reason is I did not want to go to law; I had not money to spend in law," and she seemed to be advised by her solicitors and accountants, and did not take any steps. But when this claim is made she does, and that is how the matter rests. There are a number of matters you have heard them discuss by counsel on either side again and again. I will only remind you what you have to say. You have to say whether or not it is proved to your satisfaction that the plaintiff instructed the defendants and the defendants agreed to make a complete audit. Well, I think there is only one other matter that I omitted, and that is an important one. These Balance Sheets and Profit and Loss Accounts that were sent in do not contain any signature, or any certificate by the accountants such as usually appears—"Audited and found correct." Now you heard evidence about that. Mr. Whittaker went so far as to say that because there was no such certificate it must be presumed there was not a complete audit. That, I think, is going a little too far. The other witnesses said—the plaintiff's witnesses as well as the defendants'—that when we have audited that is a certificate that we put on, and the inference, if an inference is to be drawn—as they were not put on—is that there was not a complete audit. Gentlemen, you must judge for yourselves. It is an observation in favour of the defendants that they never put it on, and they would have put it on had they been employed to audit. Therefore it all comes back to this question. You have got to consider—you have to look at the plaintiff's account and what her instructions were—whether the instructions were for a complete audit or not; and if they were, do you accept her account or Fosbrooke's account? According to his account it is quite clear that the instructions were for something different. Now you tell me upon this point whether you find for the plaintiff or for the defendant. If you are satisfied that the agreement was for a complete audit, you will find for the plaintiff; but if you find that has not been proved, then you will find for the defendant. We may have to consider hereafter, either you or me, the question of damages, but we will not

consider that at present. I will ask you to give your finding first upon the question I have put to you.

Mr. Shee: My Lord, may they have the reference to the Ledger with regard to these accounts?

Mr. Justice Bray: What reference?

Mr. Shee: Hodgson and Hill.

Mr. Justice Bray: Mr. Shee, I asked you before, and you said "No."

Mr. Shee: All right, my Lord. I agree.

The jury retired to consider their verdict.

The jury having returned,

The Associate: Now, gentlemen, have you agreed?

The Foreman: We have.

The Associate: How do you find—for the plaintiff or the defendant?

The Foreman: We find that at the creditors' meeting in London there was a distinct understanding that there was to be a complete audit.

Mr. Justice Bray: You know, you have used the words, gentlemen, that there was a distinct understanding. You know, that looks to me a distinct understanding is not an agreement. Do you find that there was an agreement for a complete audit?

The Foreman: That is so.

Mr. Justice Bray: You find that there was an agreement for a complete audit?

The Foreman: Yes; that is so, my Lord.

Mr. Justice Bray (to counsel): What do you say about damages?

Mr. Lindon Riley: What I should have liked was an answer to the question as to whether there was a contract between the plaintiff and the defendant for a complete audit.

Mr. Justice Bray (to the jury): That is what you find?

The Foreman: Yes, my Lord.

Mr. Justice Bray: Just let me have the words—what you have got down, you know, because, you see, I want to be sure. (Examined paper which was handed to him.) Oh, that will not do.

The Foreman: Well, we will retire again, my Lord.

Mr. Justice Bray: No; that will not do, gentlemen. What I must ask you—you must be really careful about this, that contract at the creditors' meeting in London—well, I must tell you that is not the contract; the contract relied upon is the contract made between the plaintiff and

Mr. Fosbrooke. I read you the evidence about it. A contract at the creditors' meeting would be a contract between somebody else ; that is what you have got to find, you know. I read you the words, you know, and you must go back please, and find, one way or the other, whether that contract is made. That is all I am leaving to you. I am not leaving to you any question of the creditors' meeting at all.

The Foreman : It is very difficult to go past the London meeting, my Lord.

Mr. Justice Bray : But you have got to find it one way or the other ; the plaintiff has got to satisfy you that the contract was made. Let me have what you have written down.

Mr. Shee : I understand that the jury do first answer the question as to whether there was an agreement or not.

Mr. Justice Bray : Well, Mr. Shee, you shall look at it, and you shall have a copy of it, and you can see what you think of it.

The jury again retired, and upon their return

The Associate : Now, gentlemen, have you agreed?

The Foreman : We have.

The Associate : Well, how do you find?

The Foreman : For the plaintiff.

Mr. Justice Bray : You find that there was a contract made on that occasion?

The Foreman : Yes, my Lord.

Mr. Justice Bray : Very well. For a complete audit?

The Foreman : Yes, my Lord.

Mr. Justice Bray : Now then, Mr. Riley, what about the question of damages?

Mr. Horridge : My Lord, I should think the best way to do would be to refer that to one of our friends to deal with, because questions may arise which are difficult with regard to it, because, if your Lordship understands, it will take up time.

Mr. Justice Bray : Well, Mr. Shee, what do you suggest? Of course, strictly speaking, you are entitled to have it decided by the jury, if you desire.

Mr. Shee : No, my Lord. I think that is a reasonable suggestion. We might agree upon somebody and mention him to your Lordship.

Mr. Justice Bray : Very well then, I will discharge the jury. You are content that the jury be discharged, Mr. Horridge?

Mr. Horridge: My Lord, I think there is no other question for them.

The Associate: Then I will formally discharge them.

Mr. Justice Bray: Then, gentlemen, you are discharged from further attendance at these assizes.

Mr. Horridge: Well, I should think that probably the best plan would be for whoever goes into the question of damages to report to your Lordship.

Mr. Justice Bray: Well, then, you know you had better agree who is to act, or, if you cannot agree anything, that I should try it—that will be the best way. You see, you have discharged the jury.

Mr. Horridge: Certainly, my Lord.

Mr. Justice Bray: Well, somebody will have to try it. If you do not agree—what do you say, Mr. Shee? Will you agree?

Mr. Shee: I should prefer that we refer it to one of our brother barristers.

Mr. Justice Bray: Well, if you do not agree, what is to happen?

Mr. Shee: I do not think we shall disagree. The question is there are so many. Very well, we can arrange that.

Mr. Justice Bray: Very well.

(34 *Acct. L.R.* 1906, p. 65.)

The case of STEVENSON *v.* BEXHILL CORPORATION.

(Decided before His Honour Judge SCULLY, in the Hastings County Court on July 9 and 30 1906.)

Elective Auditor's Duties.

This was an action brought by Mr. Joseph Henry Stevenson, one of the elective Auditors for the borough of Bexhill, against the Mayor and Corporation of Bexhill, to recover certain fees he stated he had earned in his capacity as Auditor.

Mr. Willett, in opening the case, said the action was brought by one of the elective Auditors of the borough of Bexhill to recover the sum of £19 8s. 6d., his fees as elective Auditor for the auditing of the accounts of the Corporation for the half-year ended September 30 last, at the rate of two guineas per day for 9¼ days. He (Mr. Willett) said he hoped his Honour would regard the case not so much as a matter as to whether a private individual was going to receive his salary of a number of guineas for work done honestly and to the best of his ability, but rather

as a question of great importance. Because it was a question as to whether the accounts of the Corporation were to be properly audited by the representatives of the ratepayers, or to be simply glanced over by any needy men who were content to accept any pittance the Corporation were prepared to offer them. Elective Auditors were appointed under the provisions of Section 25 of the Municipal Corporations Act, 1882, which set forth that there should be two elective Auditors elected from among the burgesses. They must be elected by the ratepayers, and must not be members of the Council. Section 26 of the Municipal Corporations Act said the Treasurer should make up his accounts half-yearly on such days as the Council with the approval of the Local Government Board appointed. Section 27 said the necessary vouchers should be submitted to the Auditors, by whom they must be audited. Schedule 5 of the Municipal Corporations Act did say that the Council had power to remunerate their officers out of the Borough Fund, but there was no specific arrangement in the Act as to the remuneration they were to pay. But the Public Health Act, 1875, Section 246, enacted that Auditors in respect of such audit should be paid such reasonable remuneration not being less than two guineas for every day of the audit. The Bexhill Council seem to have taken a very peculiar view of the meaning of that section. They seemed to have thought that they had the power to appoint the number of days the auditors should take in auditing the accounts, but he contended that if the Council had the power to appoint the number of days of each audit, the whole object of the Legislature would be nullified. Thus, the Council would be able to oust the representatives of the ratepayers, and prevent them going properly through the accounts. It seemed to him that it was quite clear that what the section meant was that the Council had the power to appoint the remuneration, but it was limited there, because it must not be less than two guineas a day. The Council could not appoint the remuneration to be one guinea a day. On September 25 1905 the Council passed a resolution to the effect that in view of the proposed engagement of a Chartered Accountant to audit the accounts of the Council, that so long as the professional audit was conducted, the Council appoint reasonable remuneration to each Auditor, the same not to exceed five guineas for each audit. That resolution, said Mr. Willett, was quite *ultra vires*, because the Council had no power to appoint the amount of the remuneration at a sum lower than two guineas a day, and they had no power to appoint the number of days the Auditors should take in the audit. He did not suggest that the Auditors should take any number of days they liked, but that was a matter for his Honour to decide. The Council contended on the case of *Thomas v. Devonport*, reported in the 1900 Law Reports, that the

Auditors were only entitled to be remunerated for that part of the accounts of the Council which related to their finances as an urban sanitary authority under the Public Health Act. In the first place, the plaintiff's claim in the present case was in contract. Mr. Stevenson had been elective Auditor for the borough of Bexhill ever since the borough was incorporated in 1902. He was first elected on March 1 1903. On every occasion since then he had always had placed before him, with the other Auditors, the whole of the accounts of the Corporation. Every book and every voucher had been placed before him regardless of whether it was necessary under the Public Health Act or not. When he had completed the audit, he had always received two guineas for every day in which he had been engaged auditing the whole of the accounts. This was done at Hastings and other towns, and Mr. Stevenson was actually paid two guineas per day ever since his election. Upon this the claim was founded. He was elected on March 1 1905, and he audited the accounts up till March 31 1905, and he was paid at the rate of two guineas per day for that. It was only on September 25 1905, a long time after his election, that any suggestion was made that the Council could pay less than the amount it was understood was to be the amount payable to the elective Auditors at the time he was elected. It was like engaging a servant for a year. He did the work for half-a-year and was paid for that, and his employer then said he would pay him less for the remainder of the year. Mr. Stevenson could not resign. His duty to the ratepayers was to do the work he had been elected to do, and therefore he considered that in contract he was entitled to claim the whole amount.

The Judge: He is dealing with the corporation of a borough. They cannot deal with him as a private individual. Their power is rather limited.

Mr. Willett said the Council had power to pay the money out of another fund. Schedule 5 of Section 19 of the Municipal Corporations Act said that the Council had power to appoint such other officers as were usually appointed in the borough or as the Council thought necessary.

Mr. Rodgers: Are you going to prove the appointment?

Mr. Willett: Do I understand the Town Clerk contends that Mr. Stevenson has never been appointed elective Auditor for the Borough of Bexhill?

The Judge: What is the section you are referring to?

Mr. Willett: I grant that it does say "officers appointed by the Council," but surely—

The Judge: This gentleman was not appointed by the Council. He is not an officer of the Council. He is the representative of the rate-payers as distinguished from an officer of the Council. His Honour then read an extract from the judgment of Lord Russell in the case of *Thomas v. Devonport*. Lord Russell said the plaintiff was not a servant of the Corporation. He was elected by the burgesses of the borough, and therefore he had no claim against the Corporation in respect of his services as elective Auditor.

Mr. Rodgers (to Mr. Willett): Do I understand that you abandon the case of contract?

Mr. Willett: If his Honour is against me—

The Judge: It is my opinion, but it does not conclude you. (Laughter.)

Mr. Willett: I prefer the case to be decided under the Public Health Act. Continuing, Mr. Willett said that in all towns there was a Borough Fund. In Devonport the rents of the corporate property went to the Borough Fund. In a modern borough like Bexhill, however, there was no Borough Fund. They had no corporate property excepting the Town Hall and the Electric Light Works. Accordingly, the amount represented by "the Borough Fund" was the minutest, and he said that any man could audit the accounts of a corporation, so far as they related to the duties of a corporation as distinct from the duties of an urban sanitary authority, in a couple of hours. The Bank Pass Books, the Treasurer's books, and the Borough Fund books, took up two pages, while the other Pass Books of the Corporation took up just 50 pages. The General District Fund Loan Account took 30 pages, the Treasurer's Borough Fund Account a paltry five pages, and the General Account 36 pages. He was not touching the Sanitary, Electric Light, and a number of other accounts.

Mr. Rodgers said he admitted that two hours was sufficient for the Borough Fund, &c., if that would help his friend.

Mr. Willett, continuing, said that the whole of the other accounts of the Corporation were, within the meaning of this section of the Public Health Act, accounts of the receipts and expenditure under this Act, and that was what they were entitled to remuneration for auditing. Mr. Willett then took the accounts of various Committees, whose works were carried out under the Public Health Act. He referred to the Cemetery, and Parks and Pleasure Grounds Committee, to the allotments of the Corporation, and the electric lighting.

The Judge asked for a table of the various heads of the audit.

Mr. Willett said he had a list of the books submitted to the elective Auditors, and supplied by the Town Clerk. The Town Clerk and he

were agreed that the only part of the audit for which they were not entitled to remuneration was the Borough Fund.

Mr. Rodgers: Quite so.

Mr. Willett: And also that it would only take two hours.

Mr. Rodgers: Yes.

The Judge: Is the real dispute as to time?

Mr. Rodgers: That is it entirely. It is a simple issue.

The Judge: It may be a simple issue as regards words, but it is not to decide. (Laughter.)

Mr. Willett said the audit had always taken three Auditors between five or seven days.

Mr. Rodgers said he gathered from his friend's opening that there was this difference between them. Mr. Willett regarded this audit as a full and ample audit of all the books of the Corporation. But the *Devonport* case showed that the audit was strictly limited. The issue was as to whether the auditors were entitled to audit more than the Borough Treasurer's accounts. The judgment of Lord Justice Russell said the audit was a strictly limited one, and was not an audit of the doings of the various Committees, but simply an audit of their Borough Treasurer as an accounting officer. Lord Justice Russell did not approve of all the language used by Mr. Justice Phillimore, but he did not in any way qualify the language which had just been read. He himself referred to the audit as an audit only of the Borough Treasurer, who was an official distinctly apart from the Corporation, and whose books were a set of books altogether outside the books of the Corporation.

Mr. Willett contended that Lord Russell's judgment did qualify this part of Justice Phillimore's remarks, when the former said the audit was incomplete and imperfect.

Mr. Rodgers: That does not in way qualify the language.

The Judge said that did not enlarge the scope of the audit as defined by Mr. Justice Phillimore. Lord Russell simply said it was within the competence of the Auditor to satisfy himself that the payments were legal and regular. He did not go beyond auditing the accounts of the Borough Treasurer.

Mr. Willett argued that that enormously extended the scope of the audit.

The Judge said of course the auditor had the right to call for evidence, but that did not enlarge the scope of the audit. It did not turn the

audit from an audit of the Treasurer's books to an audit of all the books of the Corporation.

Mr. Rodgers: That is my point.

Mr. Willett: I do submit we are bound to audit all the books of the Corporation.

Mr. Rodgers said he thought time would be saved if at that stage they decided what was the extent of the audit. Section 246 of the Public Health Act stated that where the authority was a Corporation the accounts should be audited by the borough Auditors, and the Auditors should have like duties, as if they were auditing municipal accounts. As to the type of the audit, they were referred to the Municipal Corporations Act of 1882. In Section 18 of that Act they had scarcely any reference to the accounts of the Corporation. They got nothing else beyond the accounts of an official outside the Corporation who was called a Treasurer. The Act said that every Council should appoint a Treasurer, and to show that he must be an outside official, it said the Town Clerk must not be the Treasurer. Section 25 said there must be two elective Auditors, but no reference was made as to their duties. It was Section 26 which said that the Treasurer must make up his accounts half-yearly. Section 27 said the Treasurer must submit his accounts with vouchers and papers, and the elective Auditors must audit them. So far, no reference was made to anything beyond the Treasurer's accounts. The only duty of the elective Auditors, according to an ordinary rendering of these sections, was that the audit was of the Treasurer's accounts. Mr. Rodgers proceeded to refer to the *Devonport* case, of which, he said, he had a private report which set out the case very clearly. It was sent him by the Town Clerk of Devonport.

Mr. Willett: Why not take the Law Reports?

Mr. Rodgers said the report he had simply put in plain language just the references to the sections he had given. Justice Phillimore, in the report before his Honour, said the audit was strictly limited. It was simply an audit of the accounts of the Borough Treasurer as an accounting authority. Justice Phillimore said he agreed that the Treasurer could not shut his eyes in the face of a bill which was obviously not a bill which could be passed by the Corporation. The Borough Treasurer could not shelter himself behind the three signatures. Lord Justice Russell did not agree with that sentence. The Auditor, he said, must not only look for a voucher and see that the voucher was within the province of the Council or not, but he must go a little further where there was doubt, and Lord Russell just amplified this. But it must not be suggested, argued Mr. Rodgers, from this, that Lord

Russell amplified the audit as regarded the books that were to be audited.

Mr. Willett said it was his contention that the whole of the books of the Corporation were the Treasurer's accounts; they could not distinguish between them. They could take the Postage Book, for instance.

The Judge: Surely you are dealing with the Treasurer as an accounting official

Mr. Rodgers put in certain books which he said were the Treasurer's accounts.

Mr. Willett remarked that the books put in were practically Pass Books. The Treasurer of the borough of Bexhill was manager of a bank at Lewes. To all intents and purposes the books before his Honour were nothing more or less than Bank Pass Books. They would not find any detail in them whatever. Surely the Treasurer was responsible for the accounts of the Corporation! Mr. Rodgers might as well say he was not responsible for what went on in his office.

The Judge said that, as far as the authorities read to him went, the only audit which was to be made was the audit of the Treasurer's accounts, whatever they might be.

Mr. Willett: The Treasurer is responsible for the whole of the accounts.

The Judge: He is responsible for everything he receives.

Mr. Willett: Supposing the Treasurer draws a cheque for £20 for stamps, and pays that to the Finance Clerk, who pays it to the Stamp Distribution Clerk, £5 goes here, and £5 there to the various offices. It is our duty to trace the whole of those amounts.

The Judge: To see that every stamp is duly licked and applied to the envelope. It would be absurd. His Honour added that Lord Russell only said there should be a fair and reasonable examination of the vouchers.

Mr. Willett agreed. He said they had to make a fair and reasonable examination of the payments of postage stamps. He did not say they should see every letter that was charged a penny. That was going too far.

The Judge: Can't you give me a sample instance to show how it would apply?

Mr. Willett, answering, said that in going through the Stamp Distribution Account and comparing it with the Rate Collector's account, they found a difference of £2, which had to be put right. Surely they

had to trace that. If they had not done so, that £2 would never have been discovered.

The Judge asked what were the other items in the Treasurer's accounts, and Mr. Willett said that one book on the table was the Treasurer's General Account.

Mr. Rodgers said the book was a General Cash Book belonging to the Corporation. The Treasurer had never seen it.

Mr. Willett: Then he ought to have.

Mr. Rodgers: It is a Cash Journal.

The Judge: Who keeps it?

Mr. Rodgers: The Accountant. It has never been in the Treasurer's hands. It is only a book we have to keep for Corporation purposes, and is apart altogether from there being such an office as Treasurer.

Mr. Willett: The Treasurer does not see anything of the accounts. He is only a bank manager.

Reading the section of the Act quoted by Mr. Rodgers, the Judge said it seemed that the Auditors had to audit the accounts of the Council or the Borough under the Act.

Mr. Rodgers said the section continued to the effect that the Auditors should proceed with the audit in a like manner, and have like powers and authority, and perform like duties as in the case of the audit of municipal accounts.

The Judge: I don't see how that alters the initial words of the section.

Mr. Rodgers: The audit is the audit of the Treasurer's accounts, and this fuller judgment I have here shows that.

Mr. Willett: I can't look at a judgment that is not reported in the Law Reports.

The Judge: I cannot accept notes which are not by a barrister or a solicitor.

Mr. Rodgers said that unfortunately this was a passage which bore out what he was saying.

The Judge: I cannot gather from this report whether Lord Justice Russell agrees with Justice Phillimore in saying that the accounts of the audit are simply the accounts of the Treasurer as distinct from the accounts of the Council. He differs from Justice Phillimore as to the nature of the evidence which ought to be gone into, but I cannot see that he limits in one way or another as to the scope of the audit.

Mr. Rodgers replied that Lord Russell said that but for certain words of Justice Phillimore the case would not have gone on.

Mr. Willett: Lord Russell took the view that the Borough Treasurer is responsible for the whole of the accounts. I do not know what is the distinction between the Treasurer's books, and what are not the Treasurer's books.

Mr. Rodgers: The Treasurer's books are the books the Treasurer keeps.

The Judge: The Treasurer here is simply a banker.

Mr. Rodgers: It is the practice of a number of corporations.

The Judge: How the audit could be said to be an audit of the accounts of the Council I cannot understand.

Mr. Rodgers: Our case entirely is that it is an audit of the accounts of the Borough Treasurer.

After reading Section 246 of the Act, the Judge said that how the auditor of the Bank Pass Books could be the auditor of receipts and expenditure he could not say.

Mr. Rodgers: I have here a full judgment, but your Honour does not wish it.

The Judge: I should like your judgment if I could be satisfied of the correctness of the report.

Mr. Rodgers: It comes from a litigating party.

The Judge: That makes it all the more suspicious. (Laughter.)

Mr. Rodgers then read in detail the sections of the Municipal Corporations Act which had reference to elective Auditors. Subsequently he said he agreed that if the Auditors had to do more than the Treasurer's accounts nine days was not unreasonable, but to show the absurdity of such a contention an elective Auditor would take five or six years to audit the accounts of Liverpool, or any town of importance. Also the Auditor who carried out the Devonport audit, instead of taking what Lord Justice Russell said, four days, as being ample, would have taken more than ten times that time.

Mr. Willett said they all knew that in big towns, where it was impossible for the elective Auditors to carry out the audit, they had professional Auditors. There was only one town that had turned out the elective Auditors and relied on the professionals, and that was Huddersfield.

The Judge asked where the duties of the Treasurer were defined.

Mr. Willett: Only in Sections 26 and 27.

Mr. Rodgers: No, sir. I have got something else. Section 141 says that orders of the Council for payments of moneys out of the Council

shall be signed by three members of the Council, the Town Clerk, and the Treasurer.

The Judge: Is there any provision in the Act which requires that all accounts must go to the hands of the Treasurer?

Mr. Rodgers: Section 21 covers all the accounts which officials of the Corporation receive.

The Judge: Under the Municipal Corporations Act. They could not recover anything under the Public Health Act.

Argument ensued as to what were the Treasurer's books. The General District Fund Account, the Electric Light Account, &c., were taken, and Mr. Rodgers said the Treasurer had never seen them.

The Judge: The question is, are they properly described as Treasurer's accounts? He is responsible for all receipts. All receipts of the Corporation ought to come in the hands of the Treasurer.

Mr. Rodgers: And as soon as they come there his responsibility begins.

When the question of the fuller judgment possessed by Mr. Rodgers came on again at a later stage, the Town Clerk said he did not mind having the case adjourned for the attendance of the shorthand writer who took the notes.

The Judge said he could not go outside the report he had. The case must be adjourned, or else he must reserve judgment,

Mr. Willett said the whole of the trouble had arisen through the Town Council appointing an Auditor of their own and attempting to oust the Auditors appointed by the ratepayers.

The Judge: If you make provoking statements you will be answered.

Mr. Willett: I am going to prove that the professional Auditor appointed by the Corporation came down here and took ten days to audit these very accounts. Mr. Willett added that it was the most conclusive evidence possible that an amateur had only taken nine days.

The Judge: Did the plaintiff work by himself?

Mr. Willett: The Mayor's Auditor did not come at all, because the Corporation had appointed their own professional Auditor. The two elective Auditors worked four and a-half days, and then a discussion took place between them and the Town Clerk. The result was that one of the Auditors said he was not coming again if he could not see all the books. He did not return, and the other Auditor adjourned the audit. A suggestion came from the Town Council that the audit should be resumed, and it took altogether nine days. Practically half that time Mr. Stevenson was by himself. Continuing, Mr. Willett said it would

take a great deal longer for one to undertake the audit than two, and another thing which made the audit of the accounts of the borough of Bexhill take such a great deal of time was the very meagre nature of the accounts kept.

Mr. Rodgers : Your own client says he finds the accounts in order.

Mr. Willett : I don't say they are not in order. Irregularities were discovered which were afterwards put right. Mr. Willett then read out the totals of several accounts which had nothing to show what they were for. He submitted that the consideration on account of which payment was made should have been put down.

Mr. Rodgers : The vouchers show it.

Mr. Willett : I say it is not the proper way to keep accounts. It takes a great deal longer to audit them.

The plaintiff, Mr. Joseph Henry Stevenson, was then examined. He said he lived at Brockley House, Endwell Road, and was first appointed elective Auditor in March 1903. He had been appointed ever since. Before the present audit three Auditors did the work—the Mayor's Auditor and the two elective Auditors. They all worked, and the first two audits took five days each, and the other ones six days.

Mr. Willett : Why have you taken more since then?—The books have increased since the incorporation of the town to almost double.

How long did it take the first year you audited with Mr. Thomas?—Seven days ; Mr. Thomas about five, and the Mayor's Auditor six.

You were paid two guineas for all those occasions without objection?—Yes.

What books did they produce to you?—The whole of the books of the Corporation up to date.

Could you do the work in less time?—Certainly not.

What do you say about the professional Auditor?—The Town Clerk wrote me a letter to ask me to go and see the professional Auditor. I refused to go. I contended the professional Auditor was the servant of the Corporation, and I was the servant of the ratepayers.

And when did you start auditing the accounts for the year ending September last?—On the 6th, 7th, 8th, 9th, and 10th of February, the 12th and 13th of February, and 8th and 9th of March up to the adjournment.

How long were you there on the 10th?—Up till about 7.30 in the evening. I had no assistance whatever.

What time did you start?—At 9.30.

Mr. Willett: That is the additional two hours which are going to be knocked off, your Honour. My friend and I are agreed that two hours are sufficient for the Borough Fund.

Mr. Rodgers: The Treasurer's accounts.

The Judge: The accounts relating to the Borough Fund, I understood.

Mr. Rodgers: On my system two hours would be quite sufficient for the accounts of the Treasurer.

Plaintiff, in further examination, said the relative size of the Borough Fund Accounts to the remainder was two pages to fifty.

In the aggregate Balance Sheet produced by Mr. Willett the liabilities of the Corporation District Fund Account were put at £47,047, and those of the Borough Fund at only £4,200.

The Judge: The Borough Fund might be regarded as one-tenth of the whole.

Plaintiff, continuing, said Mr. Thomas was with him four and a-half days—two and a-half days before the adjournment and the remainder afterwards.

Mr. Rodgers: Assume for the moment that these are the books you have to audit.—It would not take many minutes to audit them.

I am calling them the Treasurer's accounts. How long would it take to audit the books?—I don't call them the Treasurer's accounts.

How would you audit? This is the book which contains the largest amount of work, the District Fund Revenue Account.—That is the amount of money paid to the Treasurer and the amount paid out.

The Judge: The question is, how long would it take to audit them?

Mr. Rodgers took the plaintiff through one page of the book, and asked how he would audit it.

Plaintiff said he would find out from whence the money had been derived.

Mr. Rodgers: You call yourself an accountant?—No.

I see by a mistake you are called that in the summons, but that does not matter. How would you audit this particular entry in this book?—By going through the vouchers and particulars of that particular item. Proceeding, he said he should look to see that sums purporting to be collected had been collected.

Mr. Rodgers: If you saw the sum here tallied with the sum in the Corporation books and was shown to have been paid to the Treasurer, would that have been audited?—Certainly. I don't know exactly what you are talking about. You are wandering a bit wide.

There is no occasion to be impertinent.—If it is like the Electric Light Books, I cannot understand them, and no man could.

You know there is a book called the Allotment Rent Collector's Account?—I don't know the names of all the books you have got.

Mr. Rodgers took the plaintiff through several accounts, and Mr. Stevenson said he would require to know from whence the various amounts had come.

The Judge: Supposing your whole duty was to audit those books there, would it be sufficient for your purposes to find in that book the source from which the amounts credited in that book came?—If it was my duty to do no more than that, yes.

Mr. Rodgers: Now we have a payment to Hodgkinson of £4 11s. 4d. In checking these items you would check them with the vouchers?—Yes.

When you have seen the vouchers giving a description in respect of which each payment is made, and you have seen that Hodgkinson purports to have received a cheque, is that an audit of this payment?—I don't check them with the vouchers. I check that green book with the vouchers, and that book by the vouchers.

Tell me this, Mr. Stevenson: Are those vouchers arranged in the order in which the payments appear in that book there?—I believe they are.

Are they, or are they not?—Sometimes they are and sometimes they are not.

The general practice is for them to be arranged in that order?—The general practice is for them not to be so.

The Judge: They are not generally arranged?—They have been very much better this last twelve months.

Mr. Rodgers: Were they arranged at the last audit?—They were not.

In how many cases were they not in order?—I did not book the cases. I got through the audit as quickly as possible.

You are here to say they are not in order by the entries there.—I won't split straws with you. Don't get me to say anything that's not true, because you will not do it.

To audit fifty pages of receipts and payments with entries in the Corporation books, seeing payments to the Treasurer, and vouchers, and seeing receipts for payments, how long would it take?—There are other things to get with them.

Answer the question.—One day.

That is just what my evidence gives.—That book, I say. I am not referring to the book his Honour has got.

Assume those are the Treasurer's books, and that those are all you have to audit; would the type of audit I have put to you be a sufficient audit?—Certainly not.

There is an Allotment Rent Collector's Account. Does that account show the number of small payments from the tenants of allotments?—It does.

Does that account on the other side show by payment to the Treasurer a certain sum?—Yes.

If you turned to the General Fund Account of the Treasurer, would you expect to see this sum £4 7s. 2d. entered to correspond with this payment to the Treasurer?—Yes.

When you had seen that the Treasurer properly accounted for this payment entered into this book, would that have been an intelligent audit?—It would not without the vouchers.

The vouchers! What for?—For the receipts.

You are saying that the Treasurer should concern himself as to how so-and-so paid this or that?—I say the Treasurer does not concern himself at all. He takes the amounts paid in or out.

And if that book shows the sum paid to the Treasurer, and the Treasurer shows he has received it, is that not an intelligent audit?—For that particular book, but not for the amounts received from the allotments.

The Judge: It is not a general audit of the finances of the Corporation.

Mr. Rodgers (to plaintiff): In the Electric Light Accounts would you consider it your duty to go through the counterfoil receipt of each consumer?—Yes.

What part of your nine days was taken up in doing that? There are about 500 or 600 consumers in the town.—About a day, I should think.

There are about 500 or 600 consumers in Bexhill. Assume there were 5,000 or 10,000. How long would it take you to go through the counterfoils? Ten days?—If they were entered up like your counterfoils, it would take twenty.

Mr. Rodgers said he did not wish to go into other matters. It would not be to Mr. Stevenson's credit if he did.

Plaintiff: I wish you would.

In further cross-examination, Mr. Stevenson said he had to adjourn the audit.

The Judge: Because the counterfoil receipts were in such bad order?—Yes, sir.

Mr. Rodgers: What do you mean by that? They are in consecutive order through the books.—The collector of a particular rate signed receipts a fortnight in front of himself.

Did you report the accounts in order?—After we adjourned it, and after you put them in order.

Just to show the type of Auditor the Council have to deal with; you reported the irregular way in which the accounts were kept, and that certain items and books had been tampered with?—I did.

Did the Council ask for particulars?—Yes.

Was your reply, "We do not feel disposed to enter into any controversy over the report, and have no inclination to reply to details"?—Now I'll explain. I think his Honour should know.

The Judge: What is your explanation?

Plaintiff (to Mr. Rodgers): In consequence of your interference with the audit of the Electric Light Accounts we had to adjourn the audit. You refused to allow the collecting clerk to give us any information in the matter of £3 16s. 10d., said not to have been paid by a consumer, Mr. David Page. As we were getting information from the clerk the Town Clerk ordered him away, and refused any information whatever. We had to adjourn the audit, and found the book's pencil totals taken out. The £3 16s. 10d. had been paid four months before that.

Mr. Rodgers: Is that the explanation you refused to give to the Council? I thought you said the books were tampered with, and you refused to give an explanation even to the Council?—We refused to give anyone any explanation.

Mr. Rodgers drew the plaintiff's attention to an entry "D. Page, £3 16s. 10d., March 25 1905," and asked what was the order in which this account was entered during the audit.

Plaintiff: I say it was not marked paid until after the adjournment. You marked it paid, and then you'll find you carried that into another item and made it "£6 17s. 9d. paid," so that £3 16s. 10d. was paid twice. Mr. Page knew it was paid four months previously. I should like his Honour to see if those figures have not been scratched out.

The Judge: I am not going into that.

Mr. Rodgers put questions to the plaintiff on the assumption that the Treasurer's accounts were the only ones he had to audit, but it was some time before this assumption became clear to Mr. Stevenson. In answer to Mr. Rodgers, he said he considered it his duty to go through the counterfoils of the rates, and denied that it would take years to do this in a town with a population of 600,000. It took about three days to go through the counterfoils of the rate collector.

Mr. Rodgers: There are about 4,000 ratepayers in Bexhill?—No.

There are 3,000?—Over 3,000.

And there is a population of 15,000?—No. .

Fourteen thousand?—No. Over 13,000.

If it takes you three days to complete counterfoils of the rates, if you can calculate, will you within a day or two, assuming you are elective Auditor of Liverpool, say how long it would take?—I have never been to Liverpool.

How long would it take to get through the counterfoil receipts of some 100,000 ratepayers? Would it take some months?—Certainly not.

The plaintiff did not agree with views put forward by Mr. Rodgers as to the duties of an elective Auditor. As Mr. Rodgers proceeded, Mr. Stevenson said he did not understand, and could not answer the questions.

Mr. Rodgers: I'll read this again, and I think his Honour will see the perverseness we have to put up with at Bexhill: "It is necessary to clearly understand that an elective Auditor is not an Auditor performing duties of a purely arithmetical character." Do you understand that?—I do not. (Laughter.)

The Judge: What's the word that troubles you? "Arithmetical"? (Laughter.) Your duties are not confined merely to adding up figures and saying they correctly balance.—That's all we're concerned in—adding up figures and saying they are correct.

The Judge: Is it that only?—I take it so.

Mr. Rodgers: We are getting now to fathom an elective Auditor's intelligence. This is the view, "It is necessary to clearly understand that an elective Auditor is not an Auditor in the ordinary commercial sense, performing duties of a purely arithmetical character."—I do not understand what you mean. I understand my duties.

I'll give that up. It's too much. No, you don't understand it. "This kind of work is very useful and necessary, but is entirely beyond the power of an elective Auditor." Do you understand that?—It is nothing to do with the case.

Mr. Rodgers drew further comparisons between Bexhill and Liverpool, Hastings and Devonport, which Mr. Stevenson would not accept.

By Mr. Willett: He considered it his duty to see if payments were legal or not.

Donald Sholto Mackenzie Douglas, a member of the Bexhill Town Council, said he was Mayor's Auditor during 1904-5 and 1905-6. He took six and a-half days to audit his accounts, although on the occasion in dispute he did not audit at all. He would not say Mr. Stevenson's claim was unreasonable, considering that Mr. Thomas worked only four days, and that when three men were working together it took six days. The professional Auditor took twenty days against their total of fourteen.

Mr. Rodgers suggested that Mr. Stevenson wasted his time in doing what was not necessary.

Witness's cross-examination went to show the amount of time it would take to audit the Treasurer's accounts alone.

James Gibb said he was one of the first elective Auditors with Mr. Stevenson. He considered the claim reasonable.

Cross-examined: He considered his audit an internal check upon the financial doings of the Council.

Re-examined by Mr. Willett: It would not be satisfactory to the ratepayers if the audit consisted merely of an audit of the accounts of the Corporation as contained in the two books produced, with the vouchers.

The Judge: If their functions do extend into going into the finances of the Corporation, they must do what they have done. On the other hand, if they are confined to seeing to the Treasurer's accounts simply as an accounting person, they would not go to the extent.

Councillor H. Luntley supported the testimony of the last witness, and considered the claim perfectly reasonable.

Cross-examined: The ratepayers expected a report from the Auditors, and without going into the whole accounts the Auditors could not give one.

In his address to the Judge, Mr. Rodgers referred to the complaint that had been made that the Auditors had to audit the whole of the books. On February 2, before the audit, he wrote them a letter, in which he wished them to clearly understand that a number of books were placed before the elective Auditors purely as a matter of courtesy, and without prejudice to the proper audit. That defence was not put forward with the desire of withholding anything from the elective

Auditors. They could have the fullest examination of all books of account they wished, but the Corporation said that if the Auditors would not trust the members of the Council, if they represented to the ratepayers they were the only persons who protected the interests of the ratepayers, if they said that no one in the Town Hall was competent to see that payments and receipts were proper—

Mr. Willett: We never said anything of the kind.

Mr. Rodgers: Yes, you do. If they say they can't be expected to rely one particle on a professional audit carried out by a Chartered Accountant, the Council say, if that's the standpoint you take up it is unreasonable to expect to be paid for the time you spend on that work. Continuing, Mr. Rodgers said the Council had information that they were paying four or five times more for their elective audit than they should pay, and inquiry into the duties of elective Auditors was instituted. Assuming that four and a-half days were sufficient for a place like Devonport, two and a-half were more than ample for Bexhill. The Council found that by reducing the Auditor's fees they had the advantage of an internal check upon their finance doings from a professional accountant, and would still be able to allow to the elective Auditors time sufficient for their audit, and at a cost for the professional audit and the elective audit of what previously was more for the one. Mr. Rodgers further contended that as the Council conducted the electric lighting undertaking they should have, as other large commercial concerns, the advantage of a professional audit, and on a consideration of the duties of the elective Auditors the Council felt they were right in holding that the audit was a strictly limited one. The Town Clerk argued that in a large town the elective Auditors would be unable to institute an internal check upon the whole finances of the Corporation, as was desired in the present case, through sheer lack of time. He did not say that the elective audit was a satisfactory audit. It had been called by authorities a farce, and it was recommended in some quarters that it should be abolished. Mr. Rodgers referred at length to the sections of the Public Health Act and the Municipal Corporations Act which had been quoted. He contended that the audit was a strictly limited one, and was not an audit of the doings of the various Committees, but simply an audit of the accounts of their Borough Treasurer. Assuming that the audit was anything more than a limited one, the audit at Devonport could not have been done in four days. If the principle contended for by the plaintiff were correct, it would take ten years for two Auditors to complete the audit of a large town.

Mr. Rodgers agreed that nine days constituted a reasonable time if the full audit had to be done, and Mr. Willett agreed that two and a-half days were sufficient if the other scheme was correct.

The only witness called for the defence was Mr. Graham King. He said he was a Chartered Accountant, and had been appointed Auditor to three Corporations, in addition to being one of the Auditors of the City of London. He had audited the whole of the accounts of the Bexhill Corporation, and the finance transactions of the Council, for the six months ended September last, and he considered his audit was a check on the financial doings of the Corporation. There was not the slightest comparison between the elective Auditors' time and his. The book produced was a Cash Book of the Corporation, but he should not call it one of the Treasurer's accounts.

The Judge: Why not?—The Treasurer does not keep it. It is not kept in the Treasurer's Department.

The Judge: Does it relate to his accounts?—All the books of the Corporation relate to his accounts.

The Judge: You mean by the Treasurer's accounts only the books kept by him?—Yes.

In further examination, the witness said he had audited the Treasurer's accounts with the Cash Book and the vouchers. He accomplished the elective Auditors' audit in one and a-half days, with his clerk, and produced a time table of the time spent on the various books.

Cross-examined by Mr. Willett: He did not sign the Stamp Distribution Account. He audited it, but did not find anything wrong with it.

Mr. Willett: Did you find £2 wrong with it?—No.

Did you check it with the various accounts of the various people who have postage stamps.—No.

You didn't follow it up in any way?—Yes, I did.

How did you audit it?—I saw the names for the letters sent off, and checked it by the subsidiary books.

Did you not discover that one of the officers had received £2 for stamps and there was no entry in the Stamp Distribution Book?—Very likely not. It would be either in his hands or the finance clerk's at the end of the year.

If you had compared the book with the Stamp Books you must have found out there was £2 out?—I dare say I should have.

After further cross-examination the case was adjourned until July 30, when Judge Scully gave judgment.

JUDGMENT.

His Honour, in giving judgment, said: This is a case in which I have reserved my judgment from the last Court. Plaintiff claims the sum of £19 8s. 6d. The first point upon which plaintiff based his claim was the question of contract, and that he should be paid at the rate of two guineas a day for the time he was employed in auditing the accounts of the Bexhill Corporation. He was employed in the audit some nine and a quarter days, for which he claims to be paid at the rate of two guineas a day. As regards the question of contract, the claim for which was abandoned in the course of the argument, there was no evidence of such contract, and nothing in the circumstances which would imply contract. As regards the claim for work done as under the Public Health Acts, 1875, he is undoubtedly to be paid the two guineas a day for such time as he was employed, properly, in the prosecution of his duties as public Auditor. The whole question is made clear in the case of *Thomas v. Devonport Corporation*, and I have had an opportunity of seeing the full report in *The Law Times* since the last Court. The decision in that case plainly lays down that the Auditor under the Public Health Act is not to generally audit the finances of the Corporation, but only those of the Treasurer. No doubt on occasions it may be necessary for the Auditor to examine accounts other than those of the Treasurer, and it would be legal for the Auditors to do so, but the decision quoted clearly shows that the duties of an Auditor only refer to the examination of the Treasurer's accounts, although, if necessary, he can test any account by reference to any other accounts of the Corporation. The Auditor is not entitled to hold a general audit of the books, and as the plaintiff said he did go through the whole of the books, I am bound to hold that the greater part of the work is outside his rights. He could not have been employed in properly auditing the accounts for more than two days. The rest of the time has been spent in examining the accounts of the rate-collectors and the subsidiary accounts. Therefore I will allow the plaintiff two guineas a day for two days' work, or a total of £4 4s., this to be paid out of the £5 5s. now in Court.

The Town Clerk: May I ask your Honour for costs under scale "B"? The case is a very important one to all corporations of the country.

Mr. Willett asked his Honour to refuse costs to the Corporation. The case was in the nature of a trap, because the whole of the books were placed before the Auditors, and it was not pointed out to them that they were not entitled to go through all of them.

His Honour said he understood that they were placed before the Auditors without prejudice on the occasion of this audit.

Mr. Willett: Yes, but it was never suggested until this case was brought that they were only entitled to audit the Treasurer's books. Mr. Willett remarked that the Council paid for their law by an inclusive salary, so that the effect of giving costs to the Corporation would be that the Corporation would be making costs out of litigants.

His Honour: That might apply to profit costs.

(35 *Acct. L.R.* 1906, p. 17.)

The case of *NEWTON v. BIRMINGHAM SMALL ARMS COMPANY, LIM.*

(Decided before BUCKLEY, J., in the Chancery Division, on
June 27 1906.)

Company—Reserve Fund—“Internal Reserve Fund”—Articles of Association—Duty of Auditors Not to Disclose to Shareholders—Ultra vires—Companies Act, 1900 (63 & 64 Vict. c. 48), s. 23.

This was the trial of an action brought by Sir A. J. Newton, suing on behalf of the shareholders of the defendant company, against the company, claiming a declaration that a special resolution passed and confirmed in January and February, purporting to alter the company's articles of association by inserting provisions therein for an internal reserve fund, was *ultra vires* and invalid, and an injunction to restrain the company and its directors from acting on such resolution. The new article objected to was so far as material as follows:—“In addition and without prejudice to Articles 132 and 133” [which related to the formation of and dealing with a reserve fund] “the directors may in any year in which they shall recommend a dividend to be paid on the ordinary shares . . . of not less than 10 per cent. on the amount paid up thereon set aside (without disclosing the fact) out of the earnings or profits in such year remaining after providing the amounts necessary to pay the dividends payable on preference shares and the dividend which they recommend on the ordinary shares such a sum as they may deem necessary or desirable in the interest of the company as an internal reserve fund or as an addition to such internal reserve fund when formed, which internal reserve fund shall be held upon the terms and for the purposes following, that is to say—
(a) The internal reserve fund shall be separate from the reserve fund under Article 132, and need not be shown or disclosed by the Balance Sheet, and the directors need not give any information to the shareholders as to the amount, investment, or application thereof, or other-

wise in relation thereto, either in their report or otherwise. (b) Such internal reserve fund may be invested upon such investments (other than the shares of the company) as the directors may in their absolute discretion think fit, without their being liable for any depreciation of or loss in consequence of such investments. . . . (c) Such internal reserve fund may be used and applied at the discretion of the directors for any purpose for which the ordinary reserve fund is available, or for any purposes which the directors in their absolute discretion may consider will serve, protect, or advance the interests of the company, or preserve or promote the value of the undertaking, assets, or goodwill of the company. (d) The directors shall disclose the internal reserve fund and the amount thereof, and all additions thereto, and all other particulars in respect of the said fund to the Auditors of the company appointed by the shareholders, whose duty shall be to see that the same is applied for the purposes of the company in accordance with the provisions hereinbefore contained, but not to disclose any information with regard to the same to the shareholders or otherwise."

Mr. Buckmaster, K.C., and Mr. H. K. Newton, for the plaintiffs, contended that the new article was inconsistent with the duties as to auditing a company's accounts under Section 23 of the Companies Act, 1900. The section was almost an embodiment of the provisions of Section 7 of the Companies Act, 1879, with reference to the audit of accounts of limited banking companies. The first question was, What would the new article enable the directors to do? They could create an internal reserve as to which there was no supervision, and might use it as they thought fit.

Mr. Justice Buckley suggested that it was authorising the directors to use a secret service fund—a thing which was not unknown.

Counsel, continuing, said that perhaps such a fund had in times past been used for purposes which would be wrong in the case of a private individual. As regards companies, however, which were not banking companies, before the Act of 1900 there was no statutory requirement as to auditing. But apart from statute, the shareholders could insist on the directors' proper management of the company's affairs, and had the right to have accounts so that they might ascertain whether the management had been properly conducted. In *In re Forest of Dean Coal Mining Company* (10 Ch.D. 450) Sir George Jessel had defined the position of directors, saying:—"Directors have sometimes been called trustees, or commercial trustees, and sometimes they have been called managing partners; it does not much matter what you call them so long as you understand what their true position is, which is that they are really commercial men managing a trading concern for the benefit

of themselves and of all the other shareholders in it." Statutory rights of shareholders, such as the right to petition for winding up, and the right to dissent and be paid out on a reconstruction, could not be excluded or limited by the company's articles—*In re Peveril Gold Mines* (1898, 1 Ch. 122); *Payne v. Cork Company* (1900, 1 Ch. 308). Nor could the statutory right to have proper information under Section 23 of the Act of 1900 be excluded by those means. Section 21 of the Act required the shareholders at each annual meeting to appoint an Auditor, and if that was not done one shareholder could ask the Board of Trade to appoint an Auditor. Under Section 23 the Auditor had to report and certify, and it was not open to the company by its articles to compel an Auditor to commit a misdemeanour by disobeying the section. The new article was *ultra vires* and ought not to be allowed to be acted on.

Sir Robert Finlay, K.C., and Mr. R. J. Parker, for the company, said that to a great extent the principles put forward were not disputed. But there was no attempt to make the Auditors neglect their duty. The question was whether there was anything in the new articles inconsistent with Section 23 of the Act of 1900 and the duties thereby imposed. Before that Act there was no statutory requirement as to Balance Sheets. Section 23 did not require a Balance Sheet. It said that the Auditors must sign a certificate at the foot of the Balance Sheet, and must report on "every Balance Sheet laid before the company"; but the article did not prevent the Auditors from correctly certifying and reporting. The object of the article was to prevent information going out which might injure the company and help other concerns. It might not be expedient either to show that a loss had been made on some branch of business, or that even large profits had been made. Nor was it desirable to pay away to shareholders everything which might be distributable as dividend without laying by something for a rainy day. It was only proposed to do, with the assent of the shareholders, what was done every day without their assent. It was well known that there was a practice of writing down the value of assets so as to show a smaller margin for dividends. Each shareholder joined the company on the assumption that his rights might be altered by means of an alteration of articles. Their right to have a Balance Sheet depended on the articles, and if a Balance Sheet might be wholly dispensed with it might be dispensed with in part. An Auditor might say that on 99 points the Balance Sheet was right, but that on the hundredth point it did not give any information, because the shareholders were precluded by the articles from requiring that information. As regards rights which were not statutory, these might be controlled by the articles.

Mr. Buckmaster having replied,

His Lordship on June 20 said that he would give a written judgment.

JUDGMENT.

Mr. Justice Buckley on June 27 delivered judgment as follows:—In February last this company passed special resolutions the short substance of which is that the directors may, under defined circumstances, set aside (without disclosing the fact) out of the profits sums to form an “internal reserve fund”—a sort of secret service fund—and that this fund need not be shown in or disclosed by the Balance Sheet, and no information need be given to the shareholders as to its amount, investment, or application; that the directors may invest it as they think fit without being liable for loss in consequence of such investments; that they may apply it for any purposes which they consider will advance the interests of the company; and that, while the particulars as to this fund are to be disclosed to the Auditors, it is to be the Auditors’ duty not to disclose any information with regard to it to the shareholders or otherwise. The question for decision is whether, having regard to Sections 21 to 23 of the Companies Act, 1900, these special resolutions are *ultra vires*. The Companies Act, 1862, was silent as to accounts. Table A (which the company might or might not adopt, as it chose) contained provisions on the subject, but otherwise the Act left the matter untouched, relying, no doubt, upon the application of the ordinary principles applicable as between partners and proceeding upon the footing that the members of a company under the Act are partners in a special sort of partnership modified and governed by statutory provisions. The Companies Act, 1879, Section 7, contained, for the first time, provisions as to audit of accounts, and was confined to banking companies registered after 1879 as limited companies. The Companies Act, 1900, Sections 21 to 23, for the first time contained provisions as to the audit of the accounts of other companies under these Acts. The provisions of the Act of 1879 and those of the Act of 1900 are closely similar, though not the same; so similar, indeed, as that the reason for the difference is hard to see. The principal differences that I trace are that the Act of 1879 does, while the Act of 1900 does not, provide affirmatively for an annual audit, and that the Act of 1879 does, while the Acts of 1900 does not, provide that if there is no Auditor a meeting shall be forthwith called to elect an Auditor. As regards the former of the differences, I think that the Act of 1900 (though it does not do so expressly) yet does impliedly provide for an annual audit. Section 21, Subsection 1, requires the annual appointment of an Auditor to hold office for one year, and the Act contemplates that he will audit during his tenure of office. There will thus result an annual audit. As regards the latter difference, I find that Section 21, Subsection 2, provides for the

appointment of an Auditor by the Board of Trade on the application of any member in case an Auditor has not been appointed at the annual meeting. Neither statute contains any provision in favour of the public in the matter of publication of the accounts. The two statutes really do not differ, I think, in substance in their result. The question is how far the Act of 1900 goes in requiring for the protection of the members that the accounts shall be open to audit and that the report on them shall be made to the members. The defendants do not dispute that, if and so far as the special resolutions are inconsistent with the Act, it is the Act which must prevail. The concluding sentence of Section 23 requires that the Auditor shall state whether the Balance Sheet exhibits a true and correct view of the state of the company's affairs as shown by the books. Sir Robert Finlay argued that these words are satisfied if the Auditors report that the Balance Sheet does not exhibit a true view and that the statute does not, in these words, say that they shall report what is the true view. This is logically true as regards the language, but, in my judgment, the statute is saved from the reproach of having achieved no more than this impotent result by words earlier in that section, which provide that the Auditors are to report to the shareholders on the accounts. A report upon the accounts involves a report of the result of the accounts, and this necessarily involves, as matter of substance if not of form, the statement of a Balance Sheet or the equivalent of a Balance Sheet. There are, I agree, in the Act of 1900 no affirmative words to the effect of what I am about to state, but I think the language of the Act is sufficient to show that by implication it requires that there shall be annually an audit of accounts resulting in a Balance Sheet, to the accuracy of which the Auditors shall speak. The special resolutions in the present case provide that the Balance Sheet shall not disclose the internal reserve fund. It must therefore omit on the assets side of the Balance Sheet the assets which make up the amount standing to the credit of that fund and the *contra* item—namely, the credit balance of the fund—on the liability side. The result will be to show the financial position of the company to be not as good as in fact it is. If the Balance Sheet be so worded as to show that there is an undisclosed asset, the existence of which makes the financial position better than shown, such a Balance Sheet will not, in my judgment, be necessarily inconsistent with the Act of Parliament. Assets are often, by reason of prudence, estimated, and stated to be estimated, at less than their probably real value. The purpose of the Balance Sheet is primarily to show that the financial position of the company is at least

as good as there stated, not to show that it is not or may not be better. The provision as to not disclosing the internal reserve fund in the Balance Sheet is not, I think, necessarily fatal to the special resolutions. The Act, however, provides that the Auditors shall report to the shareholders on the accounts examined by them. These Auditors will examine, among others, the accounts of the internal reserve fund. A principal question in this case, I think, is whether it is a compliance with these words of the Act that the Auditors shall report that they have examined the accounts as to the internal reserve fund, that they are satisfied with them, and that the funds have been employed in manner authorised by the company's regulations, or whether there will be default in complying with the Act if they do not go on to say how the fund has been employed. In my judgment such a report would be a sufficient report within the Act if the Auditor is *bonâ fide* satisfied that in making this report, and nothing further, he is truly reporting as to "the true and correct view of the state of the company's affairs." But the special resolutions do not stop there. They provide that it shall be the duty of the Auditor not to disclose any information with regard to this fund to the shareholders or otherwise. It is, I think, inconsistent with the Act of Parliament that the Auditor shall be bound, even when he thinks that the true state of the company's affairs is affected by facts relating to the internal reserve fund, to withhold all information with regard to the same from the shareholders. If, for instance, the directors had invested the internal reserve fund upon investments which might involve the company under certain circumstances in enormous loss, the Act, I think, requires that the Auditor shall be at liberty and be bound to report that fact. In reporting upon the accounts submitted to them the Auditors do not, of course, report as to the details of the accounts to which they find no cause to take exception. Their duty is to call attention to that which is wrong, not to condescend upon all the details of that which is right. It is, I think, competent to the statutory majority of the shareholders to say that as to particular items of their business it is to the interest of the corporation that there shall be secrecy, and that the Auditors, who must for the purposes of their audit know all such details, shall not, unless their duty under the statute requires it, disclose such details to the members. There is no suggestion in this case that these clauses are intended to be used for any other than a legitimate purpose. Those who are engaged in commerce are familiar with the fact that undue publicity as regards the details of their trade, or as to their financial arrangements, may often be injurious to traders, having regard to the rivalry of competitors in trade, to complications

sometimes arising from strained relations between capital and labour, and the like. There are legitimate reasons for ensuring secrecy to a proper extent. It is not, I think, necessary, nor, having regard to the great utility of these Acts, is it desirable to expose persons who trade under these Acts to the necessities of a publicity from which their competitors are free unless such publicity is required to ensure commercial integrity. I am not disposed to look too closely for reasons why I should find clauses such as these to be inconsistent with the Act if I see that the true purpose of the Act is satisfied. I think, however, that these special resolutions go too far. Any regulations which preclude the Auditors from availing themselves of all the information to which under the Act they are entitled as material for the report which under the Act they are to make as to the true and correct state of the company's affairs are, I think, inconsistent with the Act. The defendants have left me in some doubt as to the exact position which they take up in the matter. They have desired to obtain the opinion of the Court upon the general question under the Act. They are entitled to do so, and this judgment I hope will put them in possession of my views on the subject, but I am not clear whether they threaten and intend to act upon the resolutions as they stand. They say, truly, that as regards the details of the resolutions, when they know the view of the Court upon the Act of Parliament, they can by further special resolutions alter their scheme so as to make it consistent with that view. There are no pleadings, so that it is only from the attitude of the defendants at the Bar that I can ascertain whether they threaten and intend to do the act against which an injunction is sought. It is not according to the practice of the Court to enjoin an act unless the defendants threaten and intend to do it. I postpone, therefore, for the moment the question of the exact form of the order so that I may hear what the defendants have to say.

Mr. R. J. Parker said that the company did not intend to act on the new article in its present form, and suggested that a declaration that it was *ultra vires* so far as inconsistent with the Act of 1900 would be sufficient. It was pointed out that there might be some difficulty in case an appeal was brought from his Lordship's judgment, and, after some discussion, his Lordship granted an injunction to restrain the company from acting on the special resolution, and ordered the company to pay the costs.

The case of BOGGIS-ROLFE v. PATTERSON.

(Decided before the Stipendiary, R. A. GILLESPIE, Esq., in the West Ham Police Court, on January 9 1907.)

Public Health Act, 1875, sec. 247—Audit of Local Authority's Accounts—Refusal by Borough Accountant to execute Declaration—Application by District Auditor for Penalty.

Adjourned summons.

Mr. Naldrett conducted the case on behalf of the Local Government Board Auditor, and Mr. Stephen Lynch appeared for the Borough Treasurer.

Mr. Naldrett, in opening the case, said the proceedings were taken under Section 247 of the Public Health Act, which provided, for the purposes of audit, that the Auditor could require the accounts to be shown and a declaration made of the correctness of the same. If the officer of the Council, in this case Mr. Patterson, refused, he was liable to a penalty of 40s. Mr. Boggis-Rolfe was appointed Auditor by the Local Government Board on July 28th 1904. On June 23rd 1906 an advertisement appeared in the *Stratford Express* giving formal notice of the audits. The accounts to be audited were those for the year ending March 31st 1906. On July 11th the audit was opened at the Education Offices, and the Borough Treasurer submitted his accounts. The audit had been adjourned from time to time, and still stood adjourned until January 10th. The accounts were very large, the expenditure amounting to £320,000. On September 11th the assistant Auditor, Mr. Hughes, verbally asked Mr. Patterson for a declaration, and the Treasurer said he would not give it. On September 17th the Borough Treasurer said he would like to have time to consider the matter, and the Auditor adjourned the audit until October 1st. Meanwhile, on September 19th, a request in writing to make a declaration as required by the Act was sent to Mr. Patterson. On October 1st Mr. Patterson could not attend, and the audit was adjourned till October 15th, and on that day the Local Government Board Auditor, Mr. Boggis-Rolfe, and the Treasurer were present, and the Auditor handed to Mr. Patterson a written request to make a declaration. He refused, and asked to be allowed to refer to the Finance Committee. The audit was then adjourned till November 5th, and the Auditor stated in the meantime that he would have to take proceedings if Mr. Patterson persisted in his refusal to make a declaration. A similar notice to the others, about the adjourned audit, was served on Mr. Patterson, and finished

up by asking him to make or sign a declaration of his accounts. Meanwhile the Auditor communicated with his solicitors, who wrote to Mr. Patterson asking, before they took further proceedings, whether he still declined to make a declaration. That was on October 24th, and on November 1st Mr. Patterson replied saying that he regretted and was somewhat surprised that Mr. Boggis-Rolfe had instructed them to take proceedings. He had done all in his power to assist him. He had no objection to making a declaration to their client at the next audit. His Worship would see that the Treasurer was quite willing to sign future accounts, and it seemed very odd that he should refuse to sign these accounts. On November 5th the Auditor and the Borough Treasurer attended the audit, and a written requisition for a declaration was handed to the Treasurer, but he again declined to make the declaration, and a few days later wrote to the Auditor's solicitors saying that he would put the matter before the Mayor, who was to be elected in a few days, and ask his advice in the matter. From that time onward no declaration had been made, and the audit still stood adjourned. The matter was one of considerable importance, as the accounts were large, involving an expenditure of upwards of £320,000. He contended that, if the Auditor required a declaration, the county officer—who in this case was Mr. Patterson—must give it. Mr. Patterson seemed willing to sign a declaration for future accounts, and it seemed inexplicable that he would not sign one now.

Mr. Gillespie: Do you admit that the audit is still in progress, Mr. Lynch?

Mr. Lynch: No, sir.

You contend it is concluded?—Yes, sir.

Mr. Naldrett: These accounts have never been allowed or signed by the Auditor. The audit stands adjourned until January 10th. The letter written to the Auditor on October 1st asked for a provisional certificate so that the Council could make a claim to the Local Government Board, the audit having been adjourned.

Mr. Horace Douglas Boggis-Rolfe then gave evidence. He said he was Auditor for the Essex audit district, and was appointed in July 1904 to audit accounts under the Education Act. He duly gave notice of the audit for July 11th, and the authorities inserted an advertisement in the *Stratford Express*. Witness opened the audit at the Education Offices, and the Borough Treasurer (Mr. Patterson) attended before him. The audit had been adjourned from time to time, and now stood adjourned from November 5th to January 10th. On September 17th he had an interview with the Borough Treasurer, and asked him to sign a

declaration. Witness explained to him that he had a form of declaration drawn up for his convenience, but Mr. Patterson was not willing to make the declaration. He asked for time to consider the matter, and witness adjourned the audit until October 1st. On September 19th witness gave him notice of the adjourned audit by registered post.

Mr. Lynch: You might take it that, from time to time, it was properly adjourned till November 5th.

Witness, continuing, said he adjourned the audit till November 5th. It was not convenient for Mr. Patterson to attend on October 1st, and witness adjourned it till October 15th, when the Treasurer attended, and witness handed him a written requirement to sign a declaration. He was not then willing to make or sign a declaration, but walked out of the room and said he wished to consult his Finance Committee. Witness then adjourned till November 5th. The declaration had not **yet** been made. The accounts were very very large, and required a large amount of examination. The usual practice was to close an audit by signing a certificate in the Ledger. He had not done so for these accounts.

Cross-examined by Mr. Lynch: Witness denied that he had completed the audit.

But you have gone through all the books?—Might I explain? When I am satisfied that the accounts are completed, then I can sign.

I put it that the only thing that is required to complete the audit is your signature?—I desired a declaration by Mr. Patterson.

Has anything been done to complete the audit since September 17th?—No.

He objected to sign that declaration on the ground that no good purpose could be served?—He did say so.

You wanted it because it would be useful in getting declarations from other authorities?—No; that was Mr. Patterson's suggestion. I said that it would make it easier for me to get other declarations if a gentleman in Mr. Patterson's position gave me a declaration.

This is one of the biggest authorities?—No. I think the Guardians might spend more. (Laughter.)

Mr. Lynch: You know much more about the Guardians than I do. Mr. Patterson said you were endeavouring to use him as a lever to get declarations from other officials. Is that not so?—He suggested that.

This is the first time you have asked Mr. Patterson to sign a declaration?—It is the first time I have audited the accounts of this authority.

You have always been friends with Mr. Patterson?—Yes; there has been no friction whatever.

He has always given you the greatest assistance?—That is so.

You told Mr. Patterson that asking for a declaration cast no reflection on him?—I did. I had no reason to believe that Mr. Patterson would present to me incomplete accounts.

You still hold the same views?—Yes, but I cannot understand the resistance to such a reasonable request.

You know that in the future he is willing to sign the declaration?—Yes.

Mr. Gillespie^e said he could not understand why Mr. Patterson was willing to give his signature to future accounts and not to these. He did not think there was the slightest imputation on his character. The Auditor said it was necessary for the purpose of the audit that he should have the declaration, and he was entitled to ask for it.

Mr. Lynch said he would submit that the declaration was not wanted for the purpose of the audit. He suggested that the audit was completed, all that was required being the signature of the Auditor.

Mr. Gillespie: But the Auditor says differently.

Mr. Lynch said that the Auditor only wanted the declaration because it would be of service to him to use as a precedent.

Mr. Lynch: Is it customary to ask for these declarations?

Mr. Boggis-Rolfe said he used his own discretion. He had on more than one occasion obtained a declaration.

Mr. Lynch thought that the mere asking for the declaration was casting a stigma on the Borough Treasurer. (To Mr. Rolfe): Do you intend making it a practice to ask for these declarations?—No, I don't; only if it is necessary.

Mr. Gillespie: He has a right to use his discretion.

Mr. Naldrett at this point announced that he was quite prepared to accept a declaration, either in the book or a separate document.

Mr. Gillespie: I have a very strong opinion that no insult was intended, and I should like to see this case come to an amicable close.

Mr. Patterson then went into the witness-box. He said that when he was asked for the declaration he asked the Auditor if there was any ground for suspicion, or was there any matter that had not been satisfactorily cleared up at the audit? Mr. Rolfe said that there was no suspicion, and added that it was not necessary to have the declaration in his case. He (Mr. Patterson) then asked why it was wanted, and

the Auditor, in a rather irritated manner, said, "My dear fellow, I tell you it is not necessary in your case." Witness said, "Then why ask for it?" and the Auditor replied, "Because it will assist me materially in obtaining it from other authorities." Witness concluded, when told by the Auditor that the accounts were satisfactory, that the audit was finished, and, as a matter of fact, the financial statement had been stamped with a hundred guinea stamp. He was quite prepared to swear on oath that the accounts were correct, and if asked at the beginning of the audit for the declaration he would have given it; but he maintained that in this instance he was asked for it in order that the Auditor might strengthen his own hands.

Mr. Gillespie: I don't think Mr. Patterson quite realises the position of the Auditor and the fact that he has absolute discretion in the matter. He (the magistrate) must hold that the audit had not been completed, for the books had not been signed by the Auditor.

Mr. Lynch asked that the magistrate would adopt the powers given him under Section 16 of the Summary Jurisdiction Act.

Mr. Naldrett: It is much more serious than that.

Mr. Gillespie said he thought the point had been an almost technical one from start to finish, and that this was not a case in which to inflict a penalty.

Mr. Naldrett: I suggest, sir, that it is very serious. A matter of £320,000 is involved.

Mr. Gillespie: I shall dismiss the summons on payment of costs.

Mr. Naldrett: That, sir, is treating the matter as a trivial offence.

Mr. Gillespie said he had given his decision, and on Mr. Patterson's giving his promise to sign the declaration he dismissed the summons on payment of ten guineas costs, in addition to the Court costs.

(36 *Actt.* L.R., 1907, p. 9.)

APPENDIX C.

THE following extract from the translation of SIR WALTER of HENLEY'S "Tretyce off Husbandry" (a manuscript work of the thirteenth century, recently printed by the Royal Historical Society) is of considerable interest, as showing the remarkable similarity of the duties of the Auditor of the present day with those of the Auditor of seven hundred years ago :—

"Buy and sell in season through the inspection of a true man or two who can witness the business, for often it happens that those who render accounts increase the purchases and diminish the sales. Have an inspection of account, or cause it to be made by someone in whom you can trust, once a year, and final account at the end of the year. View of Account is made to know the state of things, as well as the issues, receipts, sales, purchases, and expenses, and for raising money. If there is any (money), let it be raised and taken from the hands of the servants. For it often happens that servants by themselves, or others, make merchandise with their lord's money to their own profit; and if arrears appear in the final account, let them be speedily raised, for often servants are debtors themselves, and make others debtors whom they ought not—and this they do to conceal their disloyalty. Those who have the goods of others in their keeping ought to keep well four things: to love their lord and respect him; as to making profit, they ought to look on the business as their own; as to outlays, they ought to think that the business is another's. But there are few servants who keep these four things altogether, as many take, right and left, where they judge that their disloyalty will not be perceived. Look into your affairs often, and cause them to be reviewed, for those who serve you will thereby avoid the more to do wrong, and will take pains to do better.

"In the first place, he who renders account ought to swear that he will render a lawful account and faithfully account for what he has received of the goods of his lord, and that he will put nothing in his roll save what he has to his knowledge spent lawfully, and to his lord's

profit. And the clerk shall swear that he has lawfully entered in his roll what he understands his master has received of the lord's goods, and has entered nothing in the roll but what he understands may be to the profit of the lord. And then, if he has rendered account before, see how it compares; and if he is found in arrears of money, corn, or stock, put the whole in a stated money valuation, and charge it at the commencement of his roll, also charge it with receipts of rents and many other things.

"At the end of the year, when all the accounts shall have been rendered of the lands, the issues, and all expenses of the manor, take to yourself all the rolls, and by one or two of the most intimate and faithful men you have, make very careful comparison with the rolls of the accounts rendered, and of the rolls of the estimate of corn and stock, and according as they agree you shall see the industry or negligence of your servants and bailiffs.

"The lord of the manor ought to command and ordain that the accounts be heard every year, not in one place but on all the manors, for so can one quickly know everything, and understand the profit and loss. The lord ought to command the Auditors on the manors to hear the complaints and wrongs of everybody who complains of the steward or others, that full justice be done, and that the Auditors do right at their peril.

"The Auditors ought to be faithful and prudent, knowing their business, and all the points and articles of the account in rents, outlays, and returns of stock. And the accounts ought to be heard at each manor, to know the profit and loss, and then can the Auditors take inquest of the doings which are doubtful, and hear the complaints of each plaintiff and make the fines. The steward ought to be joined with the Auditors, not as head or companion of the account, but as sub-ordinate, for he must answer to the Auditors on the account for his doings, just as another. It is not necessary so to speak to the Auditors about making audits, for they ought to be so prudent, and so faithful, and so knowing in their business, that they have no need of others' teaching about things connected with the accounts."

APPENDIX D.

DEPRECIATION TABLES.

THE following Tables, which have been expressly compiled for this work, are designed to show the gross amount to be debited to Revenue annually in order to write off the requisite proportion of a lease costing £100, having any number of years unexpired.

It is contemplated that each year a corresponding entry will be made to the debit of Lease Account, and to the credit of Revenue Account, in respect of interest (at the rate stated at the head of the column) upon the balance standing to the debit of the Lease Account at the commencement of the year. For example, if a lease having 30 years unexpired is purchased for £100; then, if it is contemplated to credit Revenue Account at the rate of 5 per cent. per annum upon the reducing balance standing to the debit of the Lease Account, it will be necessary to credit that account, and debit Depreciation Account, with £6 10s. 1d. per annum. On the other hand, if the rate of interest be taken at the rate of 4 per cent., then the depreciation will be £5 15s. 8d.

The Table has been worked out to the nearest penny in each case; but, where the figures given have to be multiplied by any considerable number, it is desirable that a slight addition should be made, to compensate for the absence of fractions in the Table. In any event, it is further desirable that some substantial provision should be made to cover the cost of dilapidations at the end of the term.

No. of years unexpired	4 per cent.			5 per cent.			6 per cent.		
	£	s	d	£	s	d	£	s	d
1	104	0	0	105	0	0	106	0	0
2	53	0	5	53	15	7	54	10	10
3	36	0	9	36	14	5	37	8	1
4	27	5	5	28	4	0	28	17	2
5	22	8	11	23	1	11	23	14	10
6	19	1	6	19	14	0	20	6	9
7	16	13	3	17	5	8	17	18	4
8	14	17	1	15	9	5	16	2	1
9	13	9	0	14	1	4	14	14	1
10	12	6	7	12	18	11	13	11	9
11	11	8	2	12	0	9	12	13	7
12	10	13	0	11	5	8	11	18	7
13	10	0	2	10	12	8	11	5	11
14	9	9	5	10	2	0	10	15	2
15	8	19	10	9	12	8	10	5	11
16	8	11	8	9	4	6	9	17	11
17	8	4	4	8	17	5	9	10	10
18	7	18	0	8	11	1	9	4	8
19	7	12	3	8	5	6	8	19	2
20	7	7	2	8	0	6	8	14	4
21	7	2	7	7	16	0	8	10	0
22	6	18	5	7	11	11	8	6	1
23	6	14	7	7	8	3	8	2	7
24	6	11	2	7	4	11	7	19	5
25	6	8	0	7	1	11	7	16	6
26	6	5	1	6	19	1	7	13	10
27	6	2	5	6	16	7	7	11	5
28	6	0	1	6	14	3	7	9	2
29	5	17	9	6	12	1	7	7	2
30	5	15	8	6	10	1	7	5	4
31	5	13	8	6	8	3	7	3	7
32	5	11	10	6	6	7	7	2	0
33	5	10	2	6	5	0	7	0	8
34	5	8	8	6	3	6	6	19	3
35	5	7	2	6	2	2	6	18	0
36	5	5	9	6	0	10	6	16	9
37	5	4	6	5	19	8	6	15	8
38	5	3	3	5	18	7	6	14	9
39	5	2	2	5	17	6	6	13	10
40	5	1	1	5	16	7	6	12	11
41	5	0	1	5	15	8	6	12	1
42	4	19	2	5	14	9	6	11	4
43	4	18	3	5	13	11	6	10	8
44	4	17	4	5	13	2	6	10	0
45	4	16	6	5	12	6	6	9	5
46	4	15	9	5	11	10	6	8	10
47	4	15	0	5	11	3	6	8	3
48	4	14	4	5	10	8	6	7	9
49	4	13	8	5	10	1	6	7	4
50	4	13	1	5	9	7	6	6	11

No. of years unexpired	4 per cent.	5 per cent.	6 per cent.
	£ s d	£ s d	£ s d
51	4 12 6	5 9 1	6 6 6
52	4 11 11	5 8 7	6 6 1
53	4 11 4	5 8 2	6 5 9
54	4 10 10	5 7 9	6 5 5
55	4 10 5	5 7 4	6 5 1
56	4 10 0	5 6 11	6 4 9
57	4 9 7	5 6 7	6 4 6
58	4 9 2	5 6 3	6 4 3
59	4 8 9	5 5 11	6 4 0
60	4 8 4	5 5 7	6 3 9
61	4 8 0	5 5 4	6 3 6
62	4 7 8	5 5 1	6 3 4
63	4 7 4	5 4 10	6 3 2
64	4 7 1	5 4 7	6 3 0
65	4 6 10	5 4 4	6 2 10
66	4 6 6	5 4 1	6 2 8
67	4 6 3	5 3 11	6 2 6
68	4 6 0	5 3 9	6 2 4
69	4 5 9	5 3 7	6 2 2
70	4 5 6	5 3 5	6 2 1
71	4 5 3	5 3 3	6 1 11
72	4 5 0	5 3 1	6 1 10
73	4 4 9	5 2 11	6 1 9
74	4 4 7	5 2 10	6 1 8
75	4 4 5	5 2 9	6 1 7
80	4 3 8	5 2 1	6 1 2
85	4 2 11	5 1 7	6 0 10
90	4 2 5	5 1 3	6 0 7
95	4 2 0	5 1 0	6 0 5
100	4 1 7	5 0 9	6 0 4

APPENDIX E.

NOTES ON THE COMPANIES BILL, 1907.

AT the time that this edition is going through the press a Bill has been introduced in the House of Lords on behalf of the Government, and has already passed its second reading there, to further amend the Companies Acts. This Bill is more or less founded on the recommendations of the Departmental Committee appointed by the Board of Trade in 1905, which presented its Report in June of the following year.

If passed in its present form this Bill will, *inter alia*, require all companies not issuing a prospectus to file with the Registrar of Joint Stock Companies a statement in lieu thereof, in the form shown on p. 897. It will sanction the issue of new capital at a discount in the case of companies that have already carried on business for two years or more; and will permit vendors, and others receiving payment in money or shares from a company, to apply any part thereof in payment of any commission which would (if made by the company) have been legal under Section 8 of the Companies Act 1900. At the same time the Bill extends the operation of that section so as to make it apply in the case of a company not offering its shares to the public for subscription, provided the amount of the commission proposed to be paid is disclosed in the statement filed in lieu of a prospectus, and in the circular or notice inviting subscriptions for the shares to be issued. The payment of interest out of capital is sanctioned in the case of companies engaged in the construction of any works or buildings, or the provision of any plant, which cannot be made profitable for a lengthened period,

provided there has been due disclosure, and provided that the previous sanction of the Board of Trade has been obtained. All mortgages or charges created by a company after the Bill has become operative will require registration, perpetual debentures may be issued, an option to purchase may be granted to mortgagees, and in certain cases power will be granted to reissue debentures that have been redeemed. Power is further granted to the Court to grant relief to directors, or promoters, in certain cases, upon lines akin to those under which relief may be granted to Trustees against the consequences of inadvertent breach of trust.

The most important provisions, however, from the point of view of the present work, are those relating to Accounts and Audit, and it is because of these that it has been thought desirable to add this Appendix; for, should these Clauses be enacted in their present or some similar form, they will, it is thought, have a somewhat far-reaching effect upon the duties and responsibilities of Auditors.

The clauses referred to stood as follows after the second reading of the Bill in the House of Lords:—

AUDITORS; BALANCE SHEET; AND REPORTS.

Auditors.

21.—The following section shall be substituted for Section 23 of the Companies Act 1900:—

“(1) Every Auditor of the company shall have a right of access at all times to the books and accounts and vouchers of the company, and shall be entitled to require from the directors and officers of the company such information and explanation as may be necessary for the performance of the duties of the Auditors.

“(2) The Auditors shall make a report to the shareholders on the accounts examined by them, and on every Balance Sheet laid before the company in general meeting during their tenure of office, and the report shall state*—

“(a) *whether or not they have obtained all the information and explanations they have required; and*

* The italics indicate (roughly) the novel features of this clause.

"(b) whether, in their opinion, the Balance Sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs *according to the best of their information and the explanations given to them*, and as shown by the books of the company.

"(3) *The report shall be attached to the Balance Sheet, or there shall be inserted at the foot of the Balance Sheet a reference to the report, and the report shall be read before the company in general meeting, and shall be open to inspection by any shareholder.*

"(4) *A person, other than a retiring Auditor, shall not be capable of being appointed Auditor at an annual general meeting unless notice of an intention to nominate that person to the office of Auditor has been given by the nominator to the company not less than fourteen days, and by the company to every shareholder not less than seven days, before the annual general meeting.*

"(5) *If any copy of a Balance Sheet is issued, circulated, or published without either having a copy of the Auditor's report attached thereto or containing such reference to that report as is required by this section, the company, and every director, manager, secretary, or other officer of the company who is knowingly a party to the default, shall on conviction be liable to a fine not exceeding fifty pounds."*

Filing of Annual Statement of Affairs by Limited Companies.

22.—†Every company required to forward to the Registrar a summary under Section 26 of the Companies Act 1862 shall annually forward to the Registrar with that summary a statement of its affairs, made up to such date as may be specified in the statement, in the form of a Balance Sheet, audited by the company's Auditors, and containing a summary of its capital, its liabilities, and its assets, giving such particulars as will disclose the nature of such liabilities and assets, and how the values of the fixed assets have been arrived at, but the Balance Sheet need not include a statement of profit and loss.

Report by Directors under 63 & 64 Vict. c. 48, s. 12.

23.—†The report which the directors are required by Section 12 of the Companies Act 1900 to forward to every member of the company at least seven days before the date on which the statutory meeting of the company is held, shall contain an abstract of the receipts of the company on account of its capital, whether from shares or debentures, and of the payments made thereout, up to a date within seven days of the date of the report, exhibiting under distinctive headings the receipts of the company from shares and debentures and other sources, the pay-

† These clauses are entirely novel.

ments made thereout, and particulars concerning the balance remaining in hand, and an account or estimate of the preliminary expenses of the company.

Rights of Preference Shareholders, &c., as to Receipt and Inspection of Reports, &c.

24.—†Holders of preference shares and debentures of a company shall have the same right to receive and inspect the Balance Sheets of the company and the reports of the Auditors and other reports as are possessed by the holders of ordinary shares in the company, unless a provision to the contrary is contained in the articles of association and is disclosed in the prospectus offering the preference shares or debentures for subscription or in the statement in lieu of prospectus, or unless an express agreement to the contrary is made.

It will be observed that the amendments of Section 23 of the Companies Act 1900 contemplated by Clause 21 (reproduced above) are entirely in accordance with that which has been consistently put forward in this work, as being the most reasonable and most desirable interpretation of the admittedly vague wording of the section of the Act referred to. It is to be hoped that, whatever may be abandoned or modified, Clause 21 will be retained in the above form, thus rendering it impossible for an Auditor to report to shareholders under such circumstances that they may be led to believe that his report, and the whole of his report, appears upon the face of the Balance Sheet when in point of fact the more material portion thereof does not so appear, but is confined to an unpublished document with which the shareholders as a body have but little opportunity of becoming acquainted. In connection with this last statement it is perhaps desirable to point out that the practice has grown up of reading the Auditors' Report to the shareholders immediately after the formal notice convening the meeting has been read. The result is that it is usually read before the shareholders have settled down to the business of the meeting, and under such circumstances but few can actually hear its contents, still less grasp their significance. The provision that the Auditors' Report shall, in addition, be open to inspection by any shareholder may well prove invaluable. It would be strengthened, how-

ever, if it were provided that it should be so open to inspection at the company's registered offices for at least seven days prior to the date of the general meeting at which it is to be submitted.

The provision requiring candidates for the office of Auditor, other the the retiring Auditor, to be nominated in advance will serve the very useful purpose of making it difficult for directors who find their Auditor inconveniently exacting to arrange with their supporters upon the other side of the table to secure his removal in a quiet and unostentatious manner. Hitherto, Auditors who have come into conflict with directors in the discharge of their duty have often resigned their position rather than submit to the indignity of not being re-elected, which they knew must await them if they failed to agree with the directors, who hold the balance of the voting power. The view has always been put forward in this work that it is the duty of an Auditor, once appointed, to continue to discharge the functions of an Auditor until he has reported in general meeting to the shareholders who appointed him; but there is nothing to prevent an Auditor from retiring at any time, and there is thus nothing surprising in the fact that many professional accountants prefer to so retire, rather than to acquire—however undeservedly—the reputation of being “difficult to satisfy,” and thus impossible to deal with. With the clause as it now stands it will be necessary for those who wish to secure the removal of an Auditor to nominate in advance another willing to take his place, and it may reasonably be supposed, therefore, that such abuses will henceforward be reduced to a minimum. That they can altogether be removed is perhaps too much to hope for, seeing that, in the nature of things, while a board of directors continues in office, it may be predicted that the majority of the shareholders will support it in all its actions, presumably *inter alia* against the Auditor. This presumption seems the more reasonable when it is borne in mind that, whenever there is a conflict between directors and Auditors, it is usually because the directors seek to declare a dividend in excess of the available profits, and a disclosure

of the true position necessarily has the effect of depreciating the market value of the shares. Human nature being what it is, it is perhaps hardly to be supposed that shareholders—and particularly speculative shareholders—will go out of their way to support an Auditor in a line of action which has the direct effect of depreciating the realisable value of their property.

Clause 22, which provides that every company having its capital divided into shares shall annually file with the Registrar of Joint Stock Companies a statement in the form of a Balance Sheet, duly audited, is somewhat indefinite, inasmuch as the wording clearly permits of the filing of a statement in the form of a Balance Sheet *different to* the Balance Sheet which has actually been submitted to the company in general meeting. This appears to open the door to deceit. Bearing in mind that the Balance Sheet submitted to shareholders is itself invariably a summarised document, no possible harm could attend its publication to the whole world in that summarised form. If the filing of a more condensed form of Balance Sheet were to be permitted, the object sought to be attained by Clause 22 would in all probability not be achieved in those cases where the need for publication was greatest.

From the point of view of the Auditor, however, the special significance attaching to this clause is that it seems to throw upon him an entirely new duty; that is to say, a duty to persons *other than the shareholders of the company*, whose interests may very markedly conflict with the interests of the shareholders, or of the company itself. This enlarged duty would, it is thought, obtain even in cases where the Balance Sheet filed was invariably in the form of the Balance Sheet submitted to the company in general meeting; but if it is open to the directors to file a modified and emasculated form of Balance Sheet, the responsibility of the Auditor becomes proportionately greater. Bearing in mind that the whole object of filing such accounts is, presumably, that they may be available for the inspection of creditors, or of intending creditors or intending shareholders, it is obvious that any want of

care, or want of skill, upon the part of the Auditor would at once place him within measureable distance of the provisions of Section 84 of the Larceny Act 1861. This point is the more serious in view of the ruling of Mr. Justice BIGHAM in *Rex v. Whitaker Wright* (*vide* p. 803) as to the legal meaning of the words, "with intent to defraud or deceive."

Clause 23 is apparently intended to remove the doubts as to the true reading of Section 12 of the Companies Act 1900, which will be found referred to on p. 316. As there stated, however, before any practical value can attach to the statement required by the section referred to, it will be necessary to include not merely receipts and payments in money, but also amounts agreed to be considered as having been received on the issue of fully (or partly) paid shares and debentures, and the sums paid, either in shares or debentures, upon the acquisition of capital assets, so that the Statement of Receipts and Payments on Capital Account may be for all practical purposes a full and complete statement of the Capital Receipts and Capital Expenditure of the company, showing a balance representing the working capital that it has available for the purpose of carrying on its business.

FIRST SCHEDULE

THE COMPANIES ACTS 1862 TO 19 .
STATEMENT IN LIEU OF PROSPECTUS

filed by
Presented for filing by
LIMITED pursuant to section of the Companies Act 1904.

THE COMPANIES ACTS 1862 TO 19 .
STATEMENT IN LIEU OF PROSPECTUS.
LIMITED.

The nominal capital of the company	£	
Divided into	Shares of £ each. " " " " " "	
Names, descriptions, and addresses of directors or proposed directors.		
Minimum subscription (if any) fixed by the memorandum or articles of association on which the company may proceed to allotment.		
Number and amount of shares and debentures agreed to be issued as fully or partly paid-up otherwise than in cash. The consideration for the intended issue of such shares and debentures.	1. shares of £ 2. shares upon which £ 3. debentures 4. Consideration.	fully paid. per share credited as paid.
Names and addresses of (a) vendors of property purchased or acquired, or proposed to be (b) purchased or acquired by the company. Amount (in cash, shares, or debentures) payable to each separate vendor.		
Amount (if any) paid or payable (in cash or shares or debentures) for any such property, specifying amount (if any) paid or payable for goodwill.	Total purchase price Cash Shares Debentures Goodwill	£ £ £ £ £

Amount (if any) paid or payable as commission for subscribing or agreeing to subscribe or procuring or agreeing to procure subscriptions for any shares or debentures in the company, or	Amount paid. " payable.
Rate of such commission	Rate per cent.
Estimated amount of preliminary expenses	£
Amount paid or intended to be paid to any promoter. Consideration for such payment.	Name of promoter. Amount £. Consideration :—
Dates of, and parties to, every material contract (other than contracts entered into in the ordinary course of the business intended to be carried on by the company or entered into more than two years before the filing of this statement).	
Time and place at which such contracts or copies thereof may be inspected.	
Names and addresses of the Auditors of the company (if any).	
Full particulars of the nature and extent of the interest of every director in the promotion of or in the property proposed to be acquired by the company, or where the interest of such a director consists in being a partner in a firm, the nature and extent of the interest of the firm, with a statement of all sums paid or agreed to be paid to him or to the firm in cash or shares, or otherwise, by any person either to induce him to become, or to qualify him as, a director, or otherwise for services rendered by him or by the firm in connection with the promotion or formation of the company.	
Whether the articles contain any provisions precluding holders of preference shares or debentures receiving and inspecting Balance Sheets or reports of the Auditors or other reports.	Nature of the provisions.

(a) For definition of vendor, see Section 10 (2) of the Companies Act 1900 as amended by this Act.

(b) See Section 10 (3) of the Companies Act 1900.

We, A B., &c.

of the company hereby solemnly and sincerely declare that the statements above contained are true to the best of our knowledge information and belief, and we make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the Statutory Declarations Act 1835.

secretary of the company, and C B.,

a director [or solicitor]

MEMORANDA.

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